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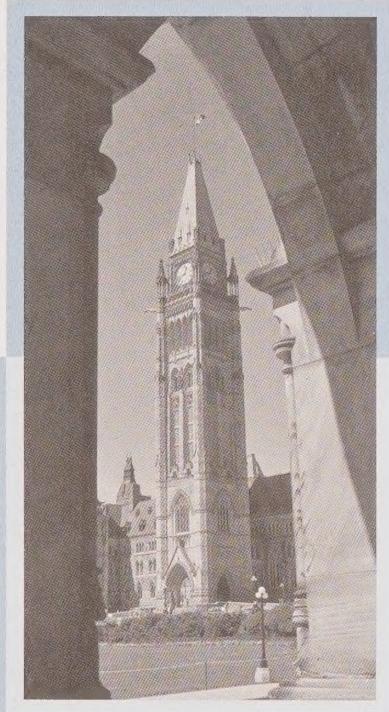
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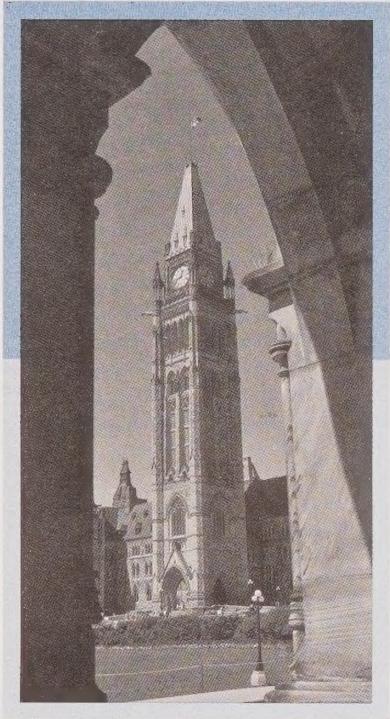
CHAPTER 1

Planning the Use of Professional Service Contractors



Office of the Auditor General of Canada

Fall 2012



Report of the Auditor General of Canada to the House of Commons

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Office of the Auditor General of Canada

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CHAPTER 1

Planning the Use of Professional Service Contractors



Performance audit reports

This report presents the results of a performance audit conducted by the Office of the Auditor General of Canada under the authority of the *Auditor General Act*.

A performance audit is an independent, objective, and systematic assessment of how well government is managing its activities, responsibilities, and resources. Audit topics are selected based on their significance. While the Office may comment on policy implementation in a performance audit, it does not comment on the merits of a policy.

Performance audits are planned, performed, and reported in accordance with professional auditing standards and Office policies. They are conducted by qualified auditors who

- establish audit objectives and criteria for the assessment of performance;
- gather the evidence necessary to assess performance against the criteria;
- report both positive and negative findings;
- conclude against the established audit objectives; and
- make recommendations for improvement when there are significant differences between criteria and assessed performance.

Performance audits contribute to a public service that is ethical and effective and a government that is accountable to Parliament and Canadians.



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Planning the Use of Professional Service Contractors

Main Points

What we examined

The need for human resources in organizations can be met by hiring additional staff or through contracting. In the federal government, professional service contractors can be engaged to meet unanticipated changes in workload and to obtain specialized expertise. This resourcing option provides managers with the necessary flexibility to meet their operational needs or to obtain expertise that is not available in a department or agency.

Professional services are usually provided by self-employed individuals or independent organizations engaged for a fixed period of time to provide expertise in such areas as information technology, management consulting, health services, and engineering and architecture. The specific conditions and details of the work to be performed are outlined in a contract.

We audited Public Works and Government Services Canada, Health Canada, and Human Resources and Skills Development Canada. Together, these departments reported that they spent just over \$2 billion on professional and special services contracts in the 2010–11 fiscal year, about 25 percent of the total amount spent government-wide on contracts in this category. We examined whether these three departments adequately plan their use of professional service contractors. We did not audit how contracts were administered and amended.

Audit work for this chapter was completed on 17 July 2012. Details on the conduct of the audit are provided in **About the Audit** at the end of the chapter.

Why it's important

The federal government spent \$8.1 billion in the 2010–11 fiscal year on professional and special services contracts with external individuals and organizations. When used strategically, professional service contractors complement the existing workforce by supplementing the knowledge and skills of public servants. Several recent audits and studies in Canada and other countries have recognized the need to strategically

manage contracted professional services, and have also raised concerns about contractors being used to complement the work of public servants on a long-term basis.

In the current environment of fiscal restraint, departments and agencies have been under pressure to reduce their expenditures and increase the flexibility of their workforce. At the same time, they need to carefully plan their use of contractors to ensure that they mitigate potential risks such as loss of corporate knowledge and in-house expertise.

What we found

- The three departments we examined plan for their need for employees and contractors separately. That is, they do not consider employee and contracting information together when making resourcing decisions. This hampers the ability of these departments to consider the full range of resourcing options available to them. As such, these departments may not be able to reassess whether the mix of employees and contractors is still optimal to achieve their business objectives. Public Works and Government Services Canada has begun to change its resource planning processes for the 2012–13 fiscal year, with a view to integrating human resource planning with other planning processes.
- Health Canada and Human Resources and Skills Development Canada primarily plan for contractor use at the project and program levels. This reduces their ability to collect or analyze information at a high enough level to fully assess departmental needs and to identify ongoing resource gaps. These two departments also conduct limited assessment of the benefits, costs, and risks of contractor use at the branch or department level.

The departments have responded. The departments agree with our recommendations. Their detailed responses follow the recommendations throughout the chapter.

Introduction

1.1 Federal departments and agencies rely on various types of human resources to deliver programs and services to Canadians. These resources include public servants who are hired for an indeterminate or temporary period of time and contractors engaged for a specified period of time. According to the Treasury Board's Contracting Policy, public service managers can engage contractors to meet unanticipated changes in workload, to obtain special expertise, or to replace an employee during temporary absences. Contractors can also be used for longer periods of time to perform ongoing work.

Professional service contractors—

Contractors who are self-employed or who work for firms. They are contracted for fixed durations to implement special projects or initiatives or provide expertise in a professional, scientific, technical, or managerial field.

Professional and special services—

All professional services performed by individuals or organizations, including the services of engineers and architects, scientific analysts, doctors, nurses, and other medical personnel, as well as consultants providing other technical, professional, and management expertise.

1.2 Professional service contractors are contractors who provide specialized expertise. The Canadian federal government spent \$8.1 billion in the 2010–11 fiscal year on professional and special services, which may also include related goods provided by individuals and organizations external to the federal government.

1.3 Government priorities may have an impact on the decision to hire employees or use contractors. For example, in his Annual Report to the Prime Minister of Canada for the 2011–12 fiscal year, the Clerk of the Privy Council indicated that departments should experiment with more nimble workforce models; they should also continue to identify tasks and functions that resources outside the public service are better placed to carry out. The Clerk also highlighted the need to continue building the public service workforce through targeted recruitment to fill gaps in key skills.

1.4 In the current climate of fiscal restraint, which requires federal organizations to curb their spending, there is an increasing need to ensure an optimal mix of resources in order to manage public funds in the most cost-effective manner. In deciding whether to hire employees or to use contractors, management must give careful consideration to a variety of factors. Strategic and well-informed decisions about the nature and mix of a department's human resources should enable the department to achieve its business objectives.

1.5 Over the past decade, the use of and spending on contractors by governments have prompted a number of countries—the United Kingdom, the United States, Australia, and New Zealand—to look at how consultants are planned for, engaged, and managed. For example, the United Kingdom Committee of Public Accounts produced a report on the topic in 2010. This Committee expressed concern that heavy reliance on contractors may indicate a lack of skills and expertise in the public service. Other concerns included questions of cost-effectiveness

and the extent to which government organizations understood the work that consultants routinely perform for the government. The Committee made a number of recommendations aimed at addressing these and related concerns.

1.6 Here in Canada, National Defence, a significant user of contractors, has recognized that there are specific challenges associated with their management. In reviews of its internal processes, the Department indicated that it did not know how many contractors it engaged and that it did not always consider and document alternatives to using professional service contractors. In 2010, the Department committed to collect basic information on contractors as well as to consider and document the human resource alternatives and decisions for high-risk contracts.

Focus of the audit

1.7 We selected three departments for this audit: Public Works and Government Services Canada, Health Canada, and Human Resources and Skills Development Canada. Together, these departments accounted for about 25 percent of the federal government's spending on professional and special services contracts in the 2010–11 fiscal year as reported in the Public Accounts of Canada (Exhibit 1.1).

1.8 The three departments we audited have very different mandates and operating environments. As a result, they have different resource needs. For example, Health Canada's regulatory mandate may require the use of highly specialized skills that are not needed on an ongoing basis. Human Resources and Skills Development Canada delivers ongoing essential programs and services to Canadians and may need contractors with technical and specialized skills to support these programs. Public Works and Government Services Canada provides its services mainly to other federal organizations and demand for its services can fluctuate, requiring some degree of resource flexibility.

1.9 The departments we audited used different types of professional and special services:

- At Public Works and Government Services Canada, most spending was for business services, engineering and architectural services, and informatics services.
- At Health Canada, most spending was for health and welfare services, scientific and research services, and management consulting services.

- At Human Resources and Skills Development Canada, most spending was for business services, informatics services, and management consulting services.

1.10 We examined the processes in place between 1 April 2010 and 31 March 2012 to see whether each of the three departments

- included information on the use of professional service contractors in organizational human resource, business, or other planning processes at the branch or departmental level; and
- based their decisions to engage professional service contractors on adequate analyses of resource options and on assessments of benefits, costs, and risks.

1.11 More details about the audit objective, scope, approach, and criteria are in **About the Audit** at the end of this chapter.

Exhibit 1.1 The departments we audited accounted for about 25 percent of federal spending on professional and special services in the 2010–11 fiscal year

| Department audited | Branches audited | Total departmental spending (\$ millions) | Percentage of total federal government spending |
|---|---|---|---|
| Public Works and Government Services Canada | <ul style="list-style-type: none"> • Real Property Branch • Translation Bureau • Parliamentary Precinct Branch • Information Technology Services Branch | \$1,167 | 14.4% |
| Health Canada | <ul style="list-style-type: none"> • First Nations and Inuit Health Branch • Health Products and Food Branch • Corporate Services Branch • Healthy Environment and Consumer Safety Branch | \$424 | 5.2% |
| Human Resources and Skills Development Canada | <ul style="list-style-type: none"> • Processing and Payment Services Branch • Skills and Employment Branch • Innovation, Information and Technology Branch • Strategic Policy and Research Branch | \$422* | 5.2% |
| Total spending by audited departments | | \$2,013 | 24.8% |
| Total spending by federal government | | \$8,130 | 100% |

*\$313 million of the \$422 million is related to the administration of federal transfer payments and delivery of nation-wide programs such as the Canada Student Loan Program. These services are provided by private sector organizations and by other levels of government.

Source: Receiver General for Canada

Observations and Recommendations

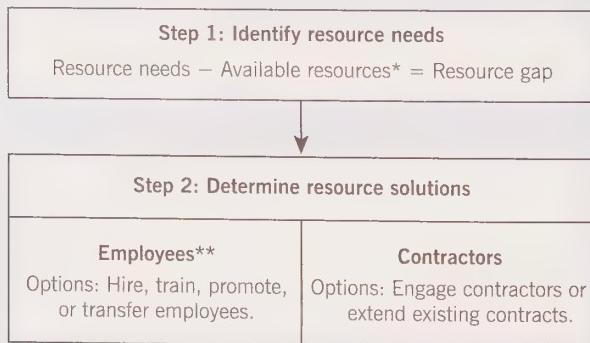
1.12 The Treasury Board and the Public Service Commission delegate authorities for human resource planning and management directly to deputy ministers. These responsibilities include having the right mix of resources in place to meet the organization's business goals. To achieve the right mix, departments must understand their current resources, gaps in skills and experience, and options to fill these gaps, including the use of contracted resources.

1.13 There is no specific guidance on how to plan for professional service contractors. However, broader policies and guidance—such as the Policy on Investment Planning, the *Financial Administration Act*, the Treasury Board Secretariat's Integrated Planning Guide, and the Privy Council Office's Guidance for Deputy Ministers—require departments and agencies to plan and manage their resources on a rational basis. Some of this guidance also highlights the importance of integrated planning.

1.14 The Treasury Board of Canada Secretariat's 2007 Integrated Planning Guide states that a resource analysis is a key component of planning. The Guide indicates that a resource analysis includes information such as demographics, skills, competencies, and the nature of the contingent workforce. The resource analysis is then used to conduct a gap analysis in order to identify resource shortages and surpluses (Exhibit 1.2).

Contingent workforce—Individuals hired or contracted on a temporary basis who are not part of the indeterminate public servant workforce. They can be temporary government employees (term, casual, and student employees), temporary help workers, or professional service contractors.

Exhibit 1.2 Resource planning process



*Available resources are current indeterminate and term employees, and professional service contractors.

**Employees can be indeterminate, term, casual, and student employees.

1.15 As market conditions and government priorities change over time, departments need to reassess whether the mix of employees and contractors is still optimal. If this mix is not carefully considered, there is a risk that functions filled by contractors will remain contracted out whether or not this is the best option. Similarly, there is a risk that functions currently staffed by employees may remain staffed without consideration of other options.

1.16 The use of contractors also involves risks that are important to assess from a branch or departmental perspective. For example, while the risk of the loss of corporate knowledge may be low when a contractor is engaged for a short time, it increases if many contractors are engaged by a branch or department for longer periods.

1.17 We examined whether the selected departments analyzed and planned their use of employees and contractors at the branch or departmental level, in an integrated manner, to meet business objectives. We examined whether this planning included an analysis of the mix of employees and contractors, information on how contractors are currently used, and how they could be used to fill identified resource gaps.

1.18 We also examined whether the departments identified and assessed the benefits, costs, and risks associated with using professional service contractors to fill resource gaps and meet business needs.

1.19 We focused on branch- and departmental-level documentation of human resource, business, and other planning, as well as information collected on contractors. We also interviewed department officials including deputy heads.

Resource planning for employees and contractors

1.20 A number of planning processes, including human resource and business planning, are used to manage department resources. Human resource planning involves analyzing the current workforce and identifying any workforce gaps to meet the current and future needs of the organization. Having the right people at the right place at the right time enables managers to carry out their projects in order to meet departmental priorities as outlined in corporate business plans. We examined branch human resource plans and business plans for the fiscal years 2010–11 and 2011–12 to see if the departments planned their use of current and future employees.

Planning for employees is not currently integrated with planning for contractors

1.21 We found that all three departments collected information on their employees as part of their human resource planning process. Information collected included employee demographic characteristics, retirement information, types of employment, occupational groups, vacancies, and employee mobility. This information was available for each branch examined in each of the three departments. The information was used to identify current in-house resource capacity and resource gaps so that each department could develop a human resource plan to meet its business objectives.

1.22 However, while the departments planned for contractors to varying degrees and at different organizational levels in the 2011–12 fiscal year (details for each department are covered in the section on planning and assessing the use of contractors), the planning for employees and contractors was not integrated. That is, they did not consider employee and contractor information together when making resourcing decisions. As a result, the departments' ability to consider the full range of resourcing options available to them is reduced. In addition, departments may not be able to assess or reassess whether they still have the best mix of employees and contractors to achieve their business objectives.

Public Works and Government Services Canada has begun to integrate planning for employees with planning for contractors

1.23 Public Works and Government Services Canada has begun to change its resource planning process for the 2012–13 fiscal year, with a view to integrating information on employees and contractors. Changes include using contracting information from the branch procurement plans in branch human resource planning.

1.24 One objective of this exercise is to help the department identify its resource requirements and an acceptable ratio between the indeterminate and flexible workforce, including resources acquired through temporary help services, standing offers, and contracts for professional services. Some of the Department's guiding principles for integrated resource planning include

- identifying core and non-core business activities;
- considering the full range of resourcing options, including contracts for professional services, to ensure a degree of flexibility in the workforce; and

- adopting a risk management approach by analyzing the risks associated with the resourcing options and their potential short-term and long-term impacts.

According to Department officials, further changes planned for the 2013–14 fiscal year should result in a more comprehensive overall human resource planning process.

1.25 We are encouraged by the steps that Public Works and Government Services Canada is taking to integrate human resource planning with other planning processes. Such integration is key for the Department to consider the full range of resourcing options, including both employees and contractors, to meet its business needs.

1.26 Recommendation. Public Works and Government Services Canada should complete the integration of its human resource planning with other relevant planning processes, and refine the integration as necessary in order to consider the full range of resourcing options to meet its business needs.

Public Works and Government Services Canada's response.

Agreed. Public Works and Government Services Canada will continue to enhance its integration of resource planning, including planning for staffing and planning for professional services. Specific direction on the requirement to consider the full range of resourcing options, including contractors, when developing resourcing strategies to meet business needs, is being developed for inclusion in the Integrated Planning Guidelines for the 2013–14 planning cycle. The Strategic Resourcing Plan will also be expanded to include more detail on the planned use of professional services and temporary help services, along with the usual planned hiring of public servants.

Health Canada and Human Resources and Skills Development Canada have yet to integrate their resource planning

1.27 At Health Canada and Human Resources and Skills Development Canada, we found that both departments plan for their need for employees and contractors separately. The branches we examined did not integrate planning of their employee requirements with their use of contractors. Managers in charge of specific projects or programs planned for employees through human resource planning and for contractors through procurement planning. We found that since human resource planning and contractor planning were not integrated, these two departments currently do not have an overall picture of their resource needs.

1.28 Health Canada. Health Canada managers indicated they are in the process of implementing an information system to collect and summarize data on employees and contractors. According to officials, this system will allow them to have a better understanding of the overall resources required to achieve the Department's business objectives in the future.

1.29 Human Resources and Skills Development Canada. Human Resources and Skills Development Canada has recognized that integrated resource planning, which includes information on the usage of contractors, is not taking place in all branches. In one directorate within a branch, we noted that the directorate relies on information technology contractors, and has recently begun to integrate information on skills and costs of contracted services as well as those of employees in order to staff resources for planned projects.

1.30 Recommendation. Health Canada and Human Resources and Skills Development Canada should take steps in their planning to bring together information on both employees and contractors in order to consider, where appropriate, the full range of resourcing options to meet their business needs.

Health Canada's response. Agreed. Health Canada intends to enhance existing practices to permit the analysis of human resource requirements and professional contracting needs as part of the integrated operational planning framework, which in turn will support management assessment of options to meet specific business needs. The plan is to have this fully implemented in the Departmental Operating Planning cycle for the 2014–15 fiscal year.

Human Resources and Skills Development Canada's response. Agreed. Human Resources and Skills Development Canada recognizes planning for business needs requires both a “top down” and “bottom up” approach, and currently plans for use of contractors at the project and program level, where much of the specific project or program design takes shape, and there is sufficient commonality of skills requirements and human resource needs to warrant this approach.

Therefore, where appropriate, the Department will review and update its 2013–14 integrated resource business planning processes and related guidelines, to ensure that the requirement to identify resources to address capacity gaps includes consideration of the full range of resourcing options, at both the branch and project or program levels.

Planning and assessing the use of contractors

1.31 Although planning for employees and contractors is not integrated, the departments we examined did plan for contractors to varying degrees and at different organizational levels. We examined whether the selected departments analyzed and planned their use of contractors at the branch or departmental level to meet business objectives. This examination included whether departments had information on how contractors are currently used, and how they could be used to fill identified resource gaps.

1.32 We also examined whether the departments identified and assessed the benefits, costs, and risks (described as follows) associated with contractor use to fill resource gaps and meet business needs.

Benefits:

- less time and effort required to identify and engage a contractor with the required knowledge and skill set compared to hiring or training an employee to perform the work;
- increased flexibility of resources—no obligation to contractor after completion of contract; and
- access unique skill sets not available in-house.

Costs:

- contractor's fees compared to the cost of training or hiring an employee to perform the work.

Risks:

- development of an employer–employee relationship, which would result in unintended benefits to the contractor and obligations on the part of the employer;
- conflict between the work-related duties and the private interests of the contractor, which could improperly influence the performance of his or her duties; and
- loss of corporate knowledge through extended reliance on a contractor, leading to an inability to benefit from the knowledge internally or to perform the work in the future.

Public Works and Government Services Canada plans for contractor use at the branch level

1.33 At Public Works and Government Services Canada, we found that all four branches we examined had identified, in their various planning processes and strategies, how professional service contractors were to be used to address resource gaps such as project management skills and service delivery functions.

1.34 We also found that three of the four branches had identified their core and non-core functions and established target ratios of employees to contractors to guide their resourcing decisions. For example, the Real Property Branch identified its real property service management and administration functions as the strategic and core activities of the branch, to be performed largely by employees. It considers its service delivery functions as non-core activities, for which it engages private sector contractors based on the target ratios it has established. The Information Technology and Services Branch also established a target ratio of 80 percent employees to 20 percent contractors based on an industry standard.

1.35 We found instances where the Department periodically reassessed decisions to use contractors in order to obtain assurance that the decisions were still valid. For example, the Department made a strategic decision in the late 1990s to contract out its real property service delivery functions. Since that time, a number of assessments were undertaken to determine whether that approach was still cost-effective.

Public Works and Government Services Canada assessed most benefits, costs, and risks related to its use of contractors

1.36 We found that Public Works and Government Services Canada has assessed most of the benefits, costs, and risks associated with its use of contractors at the branch or department level. For example, the branches we audited assessed benefits such as

- the flexibility to engage a contractor without having obligations to the contractor after completion of the contract,
- the capacity to obtain specialized expertise externally, and
- the cost-effectiveness of using contractors where employees would have to be hired or trained to do the work.

1.37 At the branch and department level, we found that Public Works and Government Services Canada has recognized the need to improve its assessment of the risks related to the creation of an employer–employee relationship. The Department has implemented a framework and additional guidelines and checklists to help managers mitigate these risks when they decide to engage contractors.

1.38 Additionally, as a result of a review of workspace use in February 2012—which included contractors—Public Works and Government Services Canada carried out an assessment of its long-term use of contractors. The review found that the Department had

almost 500 contractors who worked on its premises, of which some had been there for more than six years. A number of measures were recommended to avoid placing the Department in an employer–employee relationship with contractors. These measures included requiring the Deputy Minister’s approval when any contractor is engaged for three or more consecutive years, and properly identifying contractors in the departmental directory.

1.39 However, where the Department has relied on contractors over a period of several years, we found that the Department had done little assessment of risks related to the loss of corporate knowledge at the branch or department level. This is an important risk, particularly for functions that are largely contracted out for extended periods and for tasks requiring specialized expertise.

Health Canada and Human Resources and Skills Development Canada focus their planning for contractors at the project and program level

1.40 Planning for the use of contractors at the branch or department level is important because it allows departments to identify broader resource needs, such as skill sets required on an ongoing basis. At Health Canada and Human Resources and Skills Development Canada, we found limited resource planning for contractors at the branch or department level.

1.41 Health Canada. At Health Canada, we found that planning for contractors was done primarily at the project and program level. Managers in charge of projects and programs within each branch assessed their available resourcing options and, when applicable, identified the need for contractors in their budget. While this information was summarized, most branches did not analyze it from a branch perspective to assess whether they had the right mix of employees and contractors or to identify ongoing resource gaps.

1.42 However, for its largest branch, the First Nations and Inuit Health Branch, which accounted for 81 percent of the Department’s total spending on professional and special services contracts in the 2011–12 fiscal year, Health Canada identified the need to use contractors in its health care services and carried out a branch-level analysis of its reliance on nurses. In an effort to reduce its reliance on health care contractors, the Branch has developed strategies to recruit and retain nurses.

1.43 Human Resources and Skills Development Canada. At Human Resources and Skills Development Canada, we found that planning for contractors was done primarily at the project and program levels.

Department officials informed us that a strategic decision was made to plan the use of contractors in this way. They told us that the Department considered it appropriate to plan this way, given the small percentage of the Department's total spending that is spent on contractors.

1.44 While it has some information at the project level, we found that the Department does not collect information at a high enough level to fully assess departmental needs and gaps, and to determine if using contractors is the most cost-effective way to perform the work.

1.45 For example, the Department has identified that it has a lack of project managers and recognizes that solutions to address this need include training employees and contracting project management services. However, we found that it had not assessed the magnitude of the problem in terms of how many project managers are needed and in terms of the costs of hiring and training employees and of using contractors to fill this gap.

1.46 We also found no reference in the departmental staffing strategy about the need to recruit or retain project managers in order to help address the resource gap. Without this information, the Department will have difficulty ensuring that it has the most cost-effective solution to fill the project management resource gap.

1.47 Recommendation. Health Canada and Human Resources and Skills Development Canada should identify and collect relevant information, such as the skill sets required and those available in the employee workforce, to be able to complement their current resource planning process in order to determine resource gaps at the branch or departmental level.

Health Canada's response. Agreed. Health Canada has already started to take steps to make analytical reports on procurement and contracting practices data available to managers to support them in informed decision making.

Human Resources and Skills Development Canada's response. Agreed. Human Resources and Skills Development Canada will review its current resource business planning practices, to ensure that, where appropriate, it takes into consideration resource gaps at the branch and departmental levels. In this regard, it has initiated the following corrective actions.

As an initial step, the Department is currently conducting a capacity analysis for information technology projects for integration into the Departmental Planning cycle by 2014–15. In addition, for other

smaller thematic areas, Human Resources and Skills Development Canada plans to review data and practices already in place for planning managers at the project and program levels, to enhance the ability for more integrated decision making at the branch and departmental levels. Finally, the Department will continue to assess employee skills sets as part of its integrated human resource planning and resource allocation decisions, and take into account gaps that may be addressed through training or use of other resourcing options (for example, terms or contractors). These actions will improve the information base currently in place and will allow for a more robust assessment, identification, and integration of resourcing information.

Health Canada and Human Resources and Skills Development Canada conduct limited assessments of benefits, costs, and risks of contractor use

1.48 Assessing benefits, costs, and risks at the branch or department level is important because it enables departments to assess risks—such as over-reliance on contractors—which may not have been identified on a contract-by-contract basis.

1.49 With the exception of the First Nations and Inuit Health Branch at Health Canada, which assessed costs and risks of relying on contracted nurses, we found little assessment of benefits, costs, and risks of contractor use at the branch or department level in either department. More specifically, we did not find that benefits such as the flexibility of engaging contractors or the capacity to obtain specialized expertise had been assessed. Nor had the departments assessed potential risks related to employer–employee relationships.

1.50 We also found very limited assessment of whether using contractors was the most cost-effective way to perform the work in either department. For example, at Health Canada, we reviewed an information technology contract for a project to develop and implement an online licence application system. Technical work on this project has been contracted out since 2006 under 33 different contracts with 11 companies, for a total of \$5.2 million. Although the Department identified a resource need that could not be met with existing resources, we did not find evidence that the Department assessed other options—such as hiring or training an employee. The need for system maintenance was identified as ongoing. The Department informed us that after six years, as a result of realigning departmental priorities to save costs, it is now planning to have the maintenance work performed in-house.

1.51 We also noted another example where a project manager was engaged through a series of contracts over a 72-month period on two projects. We did not find any documented analysis that the department considered other resourcing options at the time the project manager was initially engaged for the two projects. In addition, we saw no subsequent reassessment when the contracts were renewed.

1.52 Recommendation. Health Canada and Human Resources and Skills Development Canada should assess and document relevant benefits, costs, and risks of engaging contractors and address any concerns arising from this assessment.

Health Canada's response. Agreed. Health Canada will make use of existing integrated planning processes to ensure that the risks, costs, and benefits associated with the engagement of professional service contractors are considered prior to making resourcing decisions.

For the fiscal year 2012–13 Corporate Risk Profile review, Health Canada will include risk of over-reliance on professional service contractors in its Corporate Risk Profile exercise.

Human Resources and Skills Development Canada's response. Agreed. Human Resources and Skills Development Canada recognizes the importance of ensuring clear linkages and usage of integrated information on resourcing, and will work to strengthen this element of its integrated resource business planning process. As such, it will make use of its existing integrated resource planning activities to ensure that the risks, costs, and benefits associated with the engagement of professional service contractors are identified, and better articulated and shared with managers to facilitate their resource decision making. Further, where appropriate, it will examine whether existing risk management processes and practices should be updated to include those risks related to the use of professional service contractors.

Conclusion

- 1.53** To be more flexible and cost-effective, departments need to know the extent and nature of their contracted resources and to consider and document alternatives on a regular basis. In the course of this audit, we saw evidence of good practices for determining how contractors are used to fill resource gaps, and for assessing the benefits, costs, and risks of using contractors. We also saw areas for improvement, such as the need to take into account the work performed by contractors in resource analyses.
- 1.54** We concluded that Public Works and Government Services Canada adequately planned for and assessed the benefits, costs, and risks of its contractor use at the branch or department level.
- 1.55** We concluded that planning for contractor use at the project and program levels at Health Canada and Human Resources and Skills Development Canada was not sufficient to identify the optimal solutions to fill resource gaps at the branch or department levels. We also found that these two departments conducted limited assessment of the benefits, costs, and risks of contractor use at the branch or department level.
- 1.56** The federal government has identified an increasing need for a more flexible workforce. Therefore, this is an opportune time to improve strategic planning and assessment of contractor use. While there is no guidance on how to specifically integrate planning and assessment of contractors with employees, policy direction encourages integrated planning. Departments may do so in a way that suits their business needs, given that they have different mandates and operating environments.
- 1.57** Although the findings contained in this report apply only to the departments we audited, in our opinion, it is important for other departments and agencies to be aware of the issues we have identified, and to share good practices in this area.

About the Audit

All of the audit work in this chapter was conducted in accordance with the standards for assurance engagements set by The Canadian Institute of Chartered Accountants. While the Office adopts these standards as the minimum requirement for our audits, we also draw upon the standards and practices of other disciplines.

Objective

The objective of our audit was to determine whether selected departments adequately plan their use of professional service contractors.

Scope and approach

Our audit focused on how three departments, which accounted for about 25 percent of the reported federal spending on professional service contractors, planned the use of professional service contractors. These departments are Public Works and Government Services Canada, Health Canada, and Human Resources and Skills Development Canada.

We examined how planning for professional service contractors was done at the branch level and at the department level. In each department we selected four branches, which were among the greatest users of professional service contractors in these departments, for detailed audit work:

- At Public Works and Government Services Canada, we audited the Real Property Branch, the Translation Bureau, the Parliamentary Precinct Branch, and the Information Technology Services Branch.
- At Health Canada, we audited the First Nations and Inuit Health Branch, the Health Products and Food Branch, the Corporate Services Branch, and the Healthy Environment and Consumer Safety Branch.
- At Human Resources and Skills Development Canada, we audited the Processing and Payment Services Branch; the Skills and Employment Branch; the Innovation, Information and Technology Branch; and the Strategic Policy and Research Branch.

We collected evidence through documentation review, interviews with department officials (including deputy heads), and review of planning processes.

In each department, we also examined a non-representative sample of 12 professional service contracts and associated documentation (such as business cases) to see what information was collected and if benefits, costs, and risks were assessed. Many of the contracts we reviewed were large-value contracts.

Finally, we conducted interviews with the Chief Human Resources Officer for the Government of Canada.

We did not look at planning the use of temporary help workers. We did not audit how contracts were administered and amended.

Criteria

| Criteria | Sources |
|--|---|
| <p>To determine whether selected departments adequately plan their use of professional service contractors, we used the following criteria:</p> | |
| <p>Selected departments include the use of professional service contractors in branch or departmental human resource, business, or other planning processes.</p> | <ul style="list-style-type: none"> • Policy on Investment Planning—Assets and Acquired Services, Treasury Board, 2009 • Integrated Planning Guide, Treasury Board of Canada Secretariat • 2010–11 Public Service Renewal Action Plan, Privy Council Office |
| <p>Selected departments base their decisions to hire professional service contractors on adequate resource analyses and assessments of benefits, costs, and risks.</p> | <ul style="list-style-type: none"> • Policy on Investment Planning—Assets and Acquired Services, Treasury Board, 2009 • Integrated Planning Guide, Treasury Board of Canada Secretariat ▪ Contracting Policy, Treasury Board |

Management of Public Works and Government Services Canada, Health Canada, and Human Resources and Skills Development Canada reviewed and accepted the suitability of the criteria used in the audit.

Period covered by the audit

The audit period examined was 1 April 2010 to 31 March 2012. Audit work for this chapter was completed on 17 July 2012.

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Appendix List of recommendations

The following is a list of recommendations found in Chapter 1. The number in front of the recommendation indicates the paragraph where it appears in the chapter. The numbers in parentheses indicate the paragraphs where the topic is discussed.

| Recommendation | Response |
|---|--|
| <p>Resource planning for employees and contractors</p> <p>1.26 Public Works and Government Services Canada should complete the integration of its human resource planning with other relevant planning processes, and refine the integration as necessary in order to consider the full range of resourcing options to meet its business needs. (1.23–1.25)</p> | <p>Public Works and Government Services Canada's response. Agreed. Public Works and Government Services Canada will continue to enhance its integration of resource planning, including planning for staffing and planning for professional services. Specific direction on the requirement to consider the full range of resourcing options, including contractors, when developing resourcing strategies to meet business needs, is being developed for inclusion in the Integrated Planning Guidelines for the 2013–14 planning cycle. The Strategic Resourcing Plan will also be expanded to include more detail on the planned use of professional services and temporary help services, along with the usual planned hiring of public servants.</p> |
| <p>1.30 Health Canada and Human Resources and Skills Development Canada should take steps in their planning to bring together information on both employees and contractors in order to consider, where appropriate, the full range of resourcing options to meet their business needs. (1.27–1.29)</p> | <p>Health Canada's response. Agreed. Health Canada intends to enhance existing practices to permit the analysis of human resource requirements and professional contracting needs as part of the integrated operational planning framework, which in turn will support management assessment of options to meet specific business needs. The plan is to have this fully implemented in the Departmental Operating Planning cycle for the 2014–15 fiscal year.</p> |
| | <p>Human Resources and Skills Development Canada's response. Agreed. Human Resources and Skills Development Canada recognizes planning for business needs requires both a “top down” and “bottom up” approach, and currently plans for use of contractors at the project and program level, where much of the specific project or program design takes shape, and there is sufficient commonality of skills requirements and human resource needs to warrant this approach.</p> <p>Therefore, where appropriate, the Department will review and update its 2013–14 integrated resource business planning processes and related guidelines, to ensure that the requirement</p> |

Recommendation**Response**

to identify resources to address capacity gaps includes consideration of the full range of resourcing options, at both the branch and project or program levels.

Planning and assessing the use of contractors

1.47 Health Canada and Human Resources and Skills Development Canada should identify and collect relevant information, such as the skill sets required and those available in the employee workforce, to be able to complement their current resource planning process in order to determine resource gaps at the branch or departmental level. (1.40–1.46)

Health Canada's response. Agreed. Health Canada has already started to take steps to make analytical reports on procurement and contracting practices data available to managers to support them in informed decision making.

Human Resources and Skills Development Canada's response. Agreed. Human Resources and Skills Development Canada will review its current resource business planning practices, to ensure that, where appropriate, it takes into consideration resource gaps at the branch and departmental levels. In this regard, it has initiated the following corrective actions.

As an initial step, the Department is currently conducting a capacity analysis for information technology projects for integration into the Departmental Planning cycle by 2014–15. In addition, for other smaller thematic areas, Human Resources and Skills Development Canada plans to review data and practices already in place for planning managers at the project and program levels, to enhance the ability for more integrated decision making at the branch and departmental levels. Finally, the Department will continue to assess employee skills sets as part of its integrated human resource planning and resource allocation decisions, and take into account gaps that may be addressed through training or use of other resourcing options (for example, terms or contractors). These actions will improve the information base currently in place and will allow for a more robust assessment, identification, and integration of resourcing information.

Recommendation

1.52 Health Canada and Human Resources and Skills Development Canada should assess and document relevant benefits, costs, and risks of engaging contractors and address any concerns arising from this assessment. (1.48–1.51)

Response

Health Canada's response. Agreed. Health Canada will make use of existing integrated planning processes to ensure that the risks, costs, and benefits associated with the engagement of professional service contractors are considered prior to making resourcing decisions.

For the fiscal year 2012–13 Corporate Risk Profile review, Health Canada will include risk of over-reliance on professional service contractors in its Corporate Risk Profile exercise.

Human Resources and Skills Development Canada's response. Agreed. Human Resources and Skills Development Canada recognizes the importance of ensuring clear linkages and usage of integrated information on resourcing, and will work to strengthen this element of its integrated resource business planning process. As such, it will make use of its existing integrated resource planning activities to ensure that the risks, costs, and benefits associated with the engagement of professional service contractors are identified, and better articulated and shared with managers to facilitate their resource decision making. Further, where appropriate, it will examine whether existing risk management processes and practices should be updated to include those risks related to the use of professional service contractors.

Report of the Auditor General of Canada to the House of Commons

Matters of Special Importance

Main Points—Chapters 1 to 7

Appendices

Planning the Use of Professional Service Contractors

Grant and Contribution Program Reforms

Protecting Canadian Critical Infrastructure Against Cyber Threats

Transition of Ill and Injured Military Personnel to Civilian Life

Real Property—National Defence

Transfer Payments to the Aerospace Sector—Industry Canada

Long-Term Fiscal Sustainability—Finance Canada



Report of the Auditor General of Canada to the House of Commons

CHAPTER 2

Grant and Contribution Program Reforms



Office of the Auditor General of Canada

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CHAPTER 2

Grant and Contribution Program Reforms



Performance audit reports

This report presents the results of a performance audit conducted by the Office of the Auditor General of Canada under the authority of the *Auditor General Act*.

A performance audit is an independent, objective, and systematic assessment of how well government is managing its activities, responsibilities, and resources. Audit topics are selected based on their significance. While the Office may comment on policy implementation in a performance audit, it does not comment on the merits of a policy.

Performance audits are planned, performed, and reported in accordance with professional auditing standards and Office policies. They are conducted by qualified auditors who

- establish audit objectives and criteria for the assessment of performance;
- gather the evidence necessary to assess performance against the criteria;
- report both positive and negative findings;
- conclude against the established audit objectives; and
- make recommendations for improvement when there are significant differences between criteria and assessed performance.

Performance audits contribute to a public service that is ethical and effective and a government that is accountable to Parliament and Canadians.

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Grant and Contribution Program Reforms

Main Points

What we examined

The federal government transfers money to individuals and to organizations of various types, including businesses and other governments. In 2010–11, transfer payments totalled \$158 billion. The majority of those payments—\$121 billion—were transferred to other levels of government and individuals through programs with ongoing spending authority. However, a significant portion—\$37 billion—was transferred through grant and contribution agreements. Our audit focused on grant and contribution programs.

Our last audit that focused specifically on grants and contributions was in 2006, after which an independent Blue Ribbon Panel commissioned by the President of the Treasury Board of Canada recommended that the government streamline the administrative and reporting burden on grant and contribution recipients. In May 2008, the government announced an action plan to reform the administration of grant and contribution programs.

In this audit, we examined whether the government has adequately implemented its action plan to date. We focused on the role played by the Treasury Board of Canada Secretariat (the Secretariat) in leading the reforms. We also examined selected activities undertaken in five federal organizations to implement the reforms.

Audit work for this chapter was completed on 17 July 2012. More details on the conduct of the audit are in **About the Audit** at the end of this chapter.

Why it's important

Properly planned and managed, grant and contribution programs provide an efficient means for the government to meet its policy objectives. Grants and contributions enable recipients to carry out activities that contribute to the government's objectives.

In its 2006 report, the independent Blue Ribbon Panel on Grants and Contributions concluded that fundamental change was needed to make the delivery of grants and contributions more efficient. It said that simplifying administration while strengthening accountability was both possible and necessary, and would require sustained leadership.

What we found

- To date, the federal government has adequately implemented the 2008 Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs, which is aimed at increasing efficiencies and reducing the administrative burden on recipients. However, neither the Treasury Board of Canada Secretariat nor the five organizations we examined have assessed the full impact of implementing the Government Action Plan on either their own administrative processes or the administrative burden on the recipients of their programs. Therefore, they cannot determine how much, if at all, their actions have led to streamlined administrative processes within federal organizations or a reduced administrative burden on recipients.
- The Treasury Board of Canada Secretariat actively led the implementation of the Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs. It led efforts to develop and obtained Treasury Board approval for a new Policy on Transfer Payments. The Secretariat also provided leadership and guidance to federal organizations to make the necessary changes, including coordinating activities across the government.
- The federal organizations we examined have taken action on most of their obligations under the new Policy on Transfer Payments. They have consulted with their applicant and recipient communities in re-designing their grant and contribution programs, and have begun to establish service standards.
- The organizations we examined have conducted risk assessments of their programs and their recipient communities and have assigned a risk rating to each recipient based on the assessments. However, despite the importance of these ratings in determining the controls that should be applied in each case—such as the extent of monitoring and reporting required—the Treasury Board of Canada Secretariat has not provided organizations with adequate guidance to ensure that risk ratings are accurate and remain current.

The Secretariat has responded. The Treasury Board of Canada Secretariat agrees with all of the recommendations. Its detailed responses follow the recommendations throughout the chapter.

Introduction

2.1 The Government of Canada affects the lives of Canadians in many different ways every day. The federal government passes laws and regulations, provides services, and levies taxes. It pays salaries to staff in hundreds of communities across the country, and it buys goods and services in every province and territory.

2.2 The federal government also transfers funds directly to governments, external organizations, and individuals. In the 2010–11 fiscal year, the government transferred over \$158 billion to provinces, territories, external organizations, and individuals. Major transfer payment programs with ongoing spending authority, such as the Canada Health Transfer to provinces and Old Age Security to senior citizens, accounted for \$121 billion in 2010–11. Other transfer payments paid through grant and contribution programs accounted for \$37 billion in 2010–11.

2.3 This audit focuses on the grant and contribution programs that transfer the \$37 billion to external organizations. These grant and contribution agreements enable the government to transfer funds to organizations that undertake actions consistent with the government's goals. The programs funded by federal grants and contributions range from health research and employment programs to investments in innovation. Organizations that receive government grants or contributions are working with the federal government to fulfill shared objectives.

Previous reporting on grant and contribution programs

2.4 In 2006, we reported on the federal government's management of grant and contribution programs. We noted that recipients had expressed concern about the heavy financial and administrative burden associated with applying for programs and with meeting the various requirements of these programs.

2.5 Later that year, the President of the Treasury Board commissioned an independent Blue Ribbon Panel on Grant and Contribution Programs "to recommend measures to make the delivery of grant and contribution programs more efficient while ensuring greater accountability." In its report, *From Red Tape to Clear Results*, published in December 2006, the Panel identified that there was unnecessary, unproductive, and needlessly complex reporting requirements that did not serve the interests of either government or recipients. It maintained that contribution programs were overly rigid

Grants—Transfer payments that are subject to pre-established eligibility criteria and other entitlement criteria. Grants are not subject to being accounted for by recipients and are not normally subject to audit.

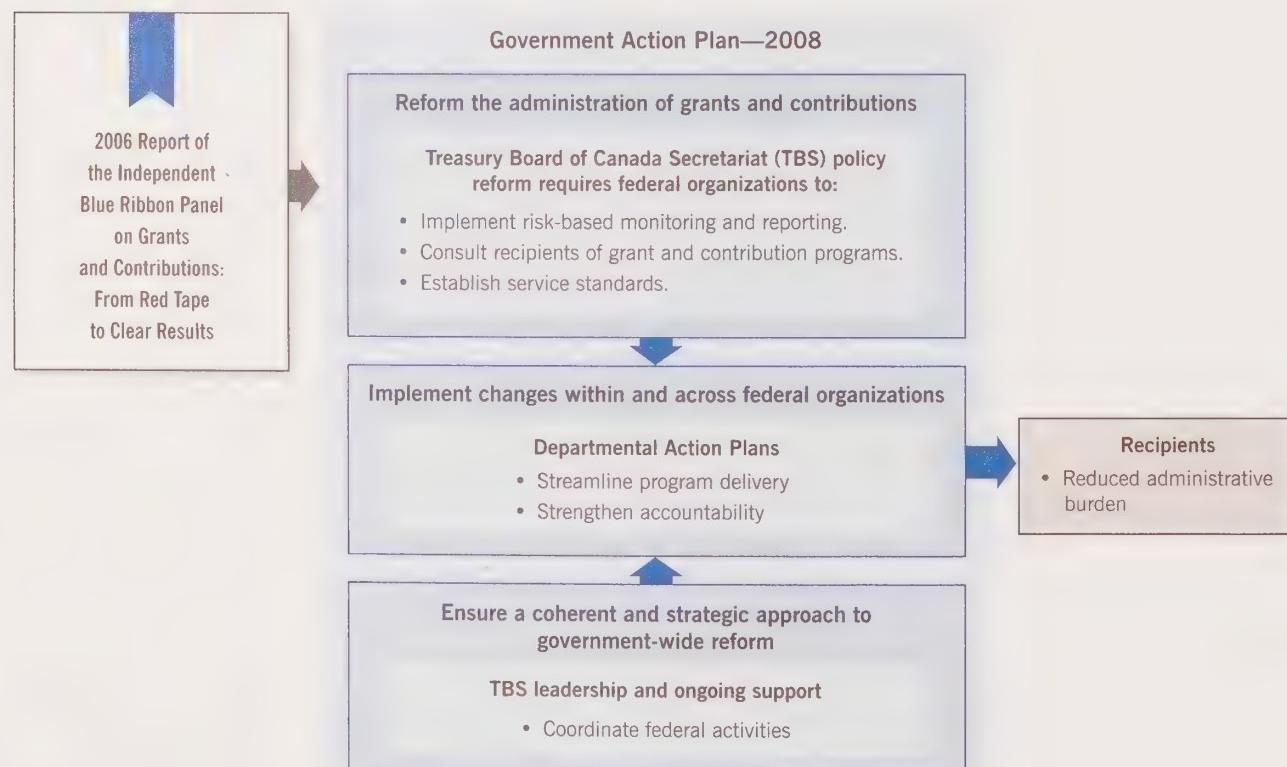
Contributions—Transfer payments that are subject to the performance conditions specified in the funding agreements. They are to be accounted for and are subject to audit.

Source: Treasury Board of Canada Secretariat

and that the government was inclined to impose a one-size-fits-all approach on recipients. The Panel concluded that the federal government needed to make fundamental changes in the way it understood, designed, managed, and reported on its grant and contribution programs. The report contained 32 specific recommendations to be implemented over the short, medium, and long term.

2.6 The federal government responded to the report of the Blue Ribbon Panel in May 2008. In its report, *The Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs*, the government indicated its intention to produce short-term results over the following three years, as well as long-term, lasting reforms that would lead to simpler processes and strengthened accountability. With the action plan, the government committed to reducing the administrative and reporting burden placed on recipients of grants and contributions. Exhibit 2.1 shows the key elements of the Government Action Plan.

Exhibit 2.1 Key elements of the 2008 Government Action Plan



Focus of the audit

2.7 This audit focuses on the implementation of the government's response to the Blue Ribbon Panel's report. Specifically, it assesses the actions of the Treasury Board of Canada Secretariat (the Secretariat) to implement the commitments made in the Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs. It also assesses the specific actions taken by the Secretariat and selected federal organizations to implement their respective obligations under the new Policy on Transfer Payments, which was developed in 2008 as part of the government's commitments in the Government Action Plan.

2.8 This audit examines selected activities related to implementing the 2008 Government Action Plan by the Treasury Board of Canada Secretariat and by the following federal government organizations: the Canadian International Development Agency, Human Resources and Skills Development Canada, Natural Resources Canada, the Public Health Agency of Canada, and Western Economic Diversification Canada. Note that the audit focus is on whether the necessary reforms were implemented and are making a difference; it does not assess whether programs are complying with all administrative, legal, and policy requirements associated with grant and contribution programs. Exhibit 2.2 identifies the federal organizations and programs we examined.

Exhibit 2.2 Federal organizations and programs examined

| Federal Organization | Program | Spending in 2011–12 (\$ millions) |
|---|--|-----------------------------------|
| Canadian International Development Agency | Tanzania Country Program To support Tanzania's national strategy for stimulating economic growth and reducing poverty, largely through enhancing access to good quality health and education services. | 67 |
| Human Resources and Skills Development Canada | Adult Learning, Literacy and Essential Skills Program To reduce non-financial barriers to lifelong learning, and to facilitate the creation of opportunities for Canadians to acquire the essential skills to fully participate in a knowledge-based economy and society. | 22 |
| Natural Resources Canada | Investments in Forest Industry Transformation (IFIT) To invest in innovative technologies in support of a more diversified, higher-value product mix in the forest sector. | 7 |
| | Non-reactor-based Isotope Supply Contribution Program (NISP) To advance research, development, and demonstration of non-reactor-based isotope technologies for medical use. | 20 |

Exhibit 2.2 Federal organizations and programs examined (continued)

| Federal Organization | Program | Spending in 2011–12 (\$ millions) |
|---|--|-----------------------------------|
| Public Health Agency of Canada | Canadian HIV Vaccine Initiative (CHVI) To contribute to global efforts to develop a safe and effective HIV vaccine. | 2 |
| Western Economic Diversification Canada | Western Diversification Program (WDP) To enhance and strengthen the economy of Western Canada by connecting research with industry's commercialization focus and by improving the business climate in Western Canada. | 68 |

2.9 We interviewed officials in selected federal organizations and collected and analyzed files, reports, and selected funding agreements. More details about the audit objectives, scope, approach, and criteria are in **About the Audit** at the end of this chapter. Note that a separate audit on contribution programs appears as Chapter 6 of this report, Transfer Payments to the Aerospace Sector—Industry Canada.

Observations and Recommendations

Implementing the Government Action Plan

2.10 The Government of Canada responded to the Blue Ribbon Panel's report with an action plan focused on policy reform, developing and implementing individual departmental action plans, and coordinating the government's grant and contribution program activities across federal organizations. The Treasury Board of Canada Secretariat (the Secretariat) was tasked with leading the federal government's reform efforts. We assessed whether the Secretariat led efforts to make the necessary changes to the Policy on Transfer Payments, supported the development and implementation of departmental action plans, and fostered a coordinated approach across the government to implement the reforms. We also assessed whether the Secretariat and selected federal organizations had determined the internal and external impacts of these reforms.

The Treasury Board of Canada Secretariat actively led the policy reform and supported the implementation of departmental action plans

2.11 Policy reform. As a first step, the government committed to reforming its Policy on Transfer Payments, requiring that the management of transfer payments be done in a manner that is sensitive

to risks. This change focuses accountability where it is most important and has the potential to reduce unnecessary administrative burden. Our audit found that the Treasury Board of Canada Secretariat led efforts to make changes to the Policy on Transfer Payments that increased flexibility for federal organizations to manage their programs based on the level of risk associated with the program, the project, and the capacity of the recipient.

2.12 The new Policy on Transfer Payments was introduced in October 2008. It clarified accountabilities for managing grant and contribution programs by clearly articulating the responsibilities of the Treasury Board, the Treasury Board of Canada Secretariat, and deputy heads of federal organizations. Some provisions were applicable immediately to all federal organizations, while others were to be phased in gradually. All provisions of the policy became applicable to all grant and contribution programs that were approved or renewed as of April 2010.

2.13 The Policy on Transfer Payments requires that the Secretariat establish a framework for reviewing the policy. We found that the Secretariat has met this requirement. It has established a process for reviewing the policy and its supporting directive, monitored its implementation, and updated the policy three times since 2008 to improve clarity. Consistent with its obligation under the policy, it has also developed a process and schedule for conducting a five-year review of the policy to begin by October 2013. We note that the process does not specify how the Secretariat plans to assess the impacts of the policy reforms.

2.14 Preparation of departmental action plans. The Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs called for federal organizations to develop their own action plans that would identify specific steps they would take to streamline and improve their grant and contribution programs. We found that the Secretariat developed an engagement strategy to encourage all federal organizations with grant and contribution programs to participate by 2011. It also encouraged organizations to identify concrete measures to improve service delivery and increase efficiency.

2.15 The Secretariat has developed an online reporting tool to collect data on actions taken by federal organizations in response to these reforms. It reported that, by June 2011, 20 federal organizations had carried out 439 separate reform actions, ranging from small administrative improvements, such as implementing direct deposit for

payments to recipients, to more comprehensive long-term measures, such as furthering interdepartmental collaboration to harmonize programs that serve the same recipients.

2.16 The Government Action Plan set out the government's objectives from June 2008 through June 2011. Recognizing that many of the activities in departmental action plans had not been fully implemented by 2011, the Secretariat committed to continue its efforts through June 2013.

The Treasury Board of Canada Secretariat fostered coordinated activities across federal organizations

2.17 In the Government Action Plan, the Treasury Board of Canada Secretariat is committed to providing leadership and ongoing support to ensure consistent implementation of new, more streamlined approaches to managing and administering grant and contribution programs across the government. To carry out this responsibility, the Secretariat has established a Centre of Expertise on Grants and Contributions (now called the Centre of Expertise on Transfer Payments) that focuses on addressing real or perceived barriers to reform, as well as promoting best practices.

2.18 Supporting interdepartmental committees. We found that the Secretariat has met this commitment through a number of initiatives. It chairs and provides support to various interdepartmental committees, including the following:

- a committee of deputy ministers who provide strategic direction,
- a committee of assistant deputy ministers who guide the implementation of reforms, and
- a committee of directors and directors general who meet monthly to develop tools for and share best practices on the implementation of their grant and contribution program reforms.

These committees are supported by working groups that lead the implementation of specific actions. Through these committees, the Secretariat has facilitated the consistency of grant and contribution programs and standardization of administrative processes.

2.19 Supporting pilot projects. We also found that the Secretariat supported pilot projects for re-structuring grant and contribution agreements. This initiative involved several federal organizations coordinating activities to develop a single comprehensive agreement with recipients that would otherwise have participated in multiple

agreements from different federal organizations. For example, one project involved seven federal departments developing a single funding agreement with a common application form and proposal guide, one contribution agreement, and a single report that met the needs of all seven organizations. As a result, the number of reports required from the recipient community for federal youth programming has been reduced from 126 to 26. Similarly, the number of up-front application and proposal forms has been reduced from 14 to 2.

2.20 Developing new tools and practices. Since 2008, the Secretariat has been working with federal organizations to develop tools and leading practices in several areas related to grant and contribution programs, including the development of guidance documents on service standards, risk management, and audits of recipients. Working with the Canada School of Public Service, the Secretariat participated in the development of a three-day training program for administrators of grant and contribution programs. Secretariat documents indicate that hundreds of public servants have taken this training.

2.21 Monitoring grant and contribution programs. The Secretariat has also monitored whether federal organizations aligned their terms and conditions of programs with the new Policy on Transfer Payments through the Treasury Board submission process for continuing or amending terms and conditions of grant and contribution programs. The Secretariat has recommended corrective actions when appropriate. In addition, the Secretariat regularly monitors certain aspects of the implementation of the policy through the annual Management Accountability Framework process.

The impact of reforms has not been assessed

2.22 The purpose of these reforms was to streamline administrative processes, strengthen accountability, and reduce the administrative and reporting burden on recipients. Recognizing this, we examined whether federal organizations had assessed changes in their own internal administrative processes and the impact of these reforms on recipients.

2.23 Specifically, we sought to determine whether federal organizations assessed their progress in streamlining their internal administrative processes. For example, this could have included tracking the level of effort involved in administering grant and contribution programs or the number of reports that had to be obtained from recipients. We found that none of the organizations we

audited had assessed the administrative impacts of reforms comprehensively, although specific areas of streamlined activities were measured by some organizations. Western Economic Diversification Canada reports that it tracked its costs of conducting recipient audits, reducing them from \$738,000 in the 2008–09 fiscal year to \$34,000 in 2011–12 by focusing audits on high-risk recipients. We also found that the Treasury Board of Canada Secretariat had not provided clear guidance to federal organizations on either the need to assess the impact of these reforms on their internal processes or how this should be done.

2.24 We also assessed whether federal organizations had determined the impact of their reforms on recipients of their programs. This is important because the impact of changes made within federal organizations is not always evident outside the government. Exhibit 2.3 demonstrates how administrative changes do not always achieve their objectives.

Exhibit 2.3 The impact of reduced reporting requirements is not always evident

The University of Victoria sought funding from Western Economic Diversification Canada (WD) for a research project to install a hybrid power system in a marine vessel donated by another organization.

The potential of this research project was considered high. Successful demonstration of this technology may lead to opportunities for a wide range of applications in the marine sector, capitalizing on zero emissions, ultra-low acoustic performance, and clean power supply.

The risks associated with this recipient were assessed as low. The low risk rating is based partly on past performance of this recipient. Over the past 11 years, with funding from WD, the University of Victoria has completed, or has in progress, 57 other projects totalling approximately \$8 million. Each of these projects has been completed or is progressing in a satisfactory manner.

The low rating for the risk assessment of this project meant that WD did less monitoring and less documentation. It reduced the number of invoices and proofs of payment to be submitted by the university, while maintaining the right to obtain these records in the future. While the reporting requirements were reduced, the university has yet to notice a significant reduction in its administrative burden.

2.25 We found that neither the Secretariat nor the other federal organizations we examined had assessed the impact of their actions on recipient organizations. While the Secretariat has gathered some data from federal organizations on their reform efforts, neither the Secretariat nor the federal organizations we examined know whether recipients have seen a reduction in their administrative burden. In fact, the information gathered by the Secretariat led to a conclusion that, despite progress, recipients had not yet felt the impact of reforms

sufficiently. As well, in November 2011, recipient organizations of the Canadian International Development Agency's grant and contribution programs complained about excessive delays in the Agency's decisions on whether or not funding applications were approved. Information on the impacts of these reforms would support the Secretariat in its planned review of the Policy on Transfer Payments.

2.26 Recommendation. The Treasury Board of Canada Secretariat should strengthen its process for gathering government-wide results-based information from federal organizations on the internal administrative impact of their activities in support of the Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs. It should also assess the impact to date on recipients' administrative burden associated with implementing the Government Action Plan. Results of this assessment should be made available publicly and be used in support of preparing the five-year review of the Policy on Transfer Payments.

The Secretariat's response: Agreed. In collaboration with federal organizations, the Secretariat will implement, in 2012 and 2013, a new results-based reporting tool to collect information on the impact, on recipients and departments, of the efforts to reform the administration and delivery of grant and contribution programs. Results of the whole-of-government assessment will be publicly available to coincide with the conclusion of the Secretariat's implementation of the Government Action Plan, and will be considered as part of the five-year review of the Policy on Transfer Payments.

Implementing policy reforms

2.27 The policy reforms established by the Treasury Board of Canada Secretariat through the Policy on Transfer Payments were aimed at ensuring that grant and contribution programs are citizen-focused and managed with integrity, transparency, and accountability in a manner that is sensitive to risks.

2.28 To assess whether the implementation of these policy reforms was leading to the intended changes in the management of government grant and contribution programs, we selected programs from each of the five federal organizations in our audit (see paragraph 2.8) and assessed whether key elements in the policy had been implemented.

2.29 Specifically, we assessed whether the organizations had developed a process to identify the risks associated with the programs, projects, and recipient organizations, whether they had modified their oversight based on risks identified, and whether they had implemented

processes to ensure that the risk ratings were appropriate and current. We also assessed whether the organizations had consulted their client populations and whether they had established service standards.

2.30 We did not assess whether all of the requirements of the Policy on Transfer Payments were implemented in all federal organizations or in all programs within the federal organizations we examined. Nor did we assess whether the management of the programs we looked at complied with all of the legislative and policy requirements for these programs.

Monitoring and reporting requirements are focused on risks, but improvements are needed

2.31 One of the key changes resulting from the new Policy on Transfer Payments is the flexibility it provides to deputy heads to tailor grant and contribution activities to the risks associated with the program, the project, and the recipients. The new policy requires that federal organizations adjust their monitoring and reporting activities to reflect their risk assessments.

2.32 Administered properly, this provision of the policy offers the potential to reduce the administrative burden for both the government and recipients. This approach is consistent with previous recommendations from our Office. Programs with projects that are well understood, and recipient partners that have a long and positive track record working with the government, should benefit from lighter monitoring and reporting requirements.

2.33 We examined departmental processes to assess and rate risks, and to determine the monitoring and reporting requirements associated with those risks. We selected sample files from each organization to confirm whether risk ratings were completed as designed, and whether monitoring and reporting requirements were consistent with the federal organization's program design.

2.34 Monitoring and reporting in relation to risks. According to the Policy on Transfer Payments, all new and continued grant and contribution programs approved after 31 March 2010 had to establish and apply a risk rating for each agreement and ensure that reporting requirements reflected the risk assessment. We found that all five federal organizations we examined had developed criteria for evaluating risks, had created risk scales, and had applied a risk rating for each recipient. Each risk assessment took into account the capacity and track record of the recipient. This process was intended to facilitate a reduction in the number of reports that low-risk recipients

were required to provide. It also meant that low-risk recipients were to be subject to fewer on-site monitoring visits and audits.

2.35 We found that monitoring and reporting requirements were clearly linked to risk assessments in the programs of three of the federal organizations we examined. Conversely, the Public Health Agency of Canada had not used the risk rating to adjust reporting requirements or monitoring activities for some of the funding agreements we looked at in the program we examined. In May 2012, subsequent to our review of its files, the Agency introduced a new tool to link reporting and monitoring requirements based on identified risks. We have not assessed the effectiveness of this tool.

2.36 The Canadian International Development Agency initiated pilot projects to link risk ratings with reporting requirements in fall 2010. At the time of our audit, the Agency had not yet linked its risk assessments of recipients with reporting requirements of the agreements we examined; however, it introduced a tool for doing so in April 2012. We have not assessed the effectiveness of this tool.

2.37 **Organizational controls.** By focusing administrative efforts where risks are high, the Policy on Transfer Payments is intended to reduce the administrative burden on low-risk recipients while ensuring that there are appropriate controls to ensure that expenditures meet program objectives and conditions. We examined how selected federal organizations maintained adequate controls to manage their programs.

2.38 One of the requirements of the Policy on Transfer Payments is that federal organizations conduct audits and reviews of their programs to ensure that proper controls, monitoring, and performance measurement processes are in place. We found that each of the federal organizations had conducted evaluations and audits of their grant and contribution programs.

2.39 In general, these audits and evaluations found that risk assessments were conducted for both the programs and the recipients and that controls and monitoring were in place. However, they also pointed to the need to improve performance information, so that risk ratings of recipients could be used to focus efforts on recipient audits. These reviews also pointed to the need for federal organizations to track changes in the efficiency of their programs.

2.40 Another requirement of the Policy on Transfer Payments is that federal organizations conduct audits of recipients, commensurate with the levels of risks identified, and that claims information be assessed before payments are issued. We assessed whether appropriate

documentation and audits were conducted for 38 grant and contribution agreements in the programs we examined. We found that the five federal organizations we examined had obtained appropriate documentation and had conducted audits for the 8 agreements where audits were warranted. We also found that the organizations appropriately assessed the documents submitted to them prior to issuing payments.

2.41 Recognizing that the ratings from risk assessments of programs and recipients are central to determining the controls that should be applied, we examined how federal organizations ensure that their risk ratings are accurate. Although not specifically a policy requirement, we examined whether federal organizations reviewed and challenged their original risk assessments.

2.42 We found that all the organizations we examined had some form of review and challenge function of their original risk ratings, although each had different processes and levels of depth in their reviews. We noted that the Secretariat does not provide federal organizations with adequate guidance for developing a review and challenge function to support organizations' risk assessment processes.

2.43 Similarly, while the policy does not require periodic reassessments of multi-year agreements, we examined how federal organizations ensure that risk assessments remain current. This is particularly important for agreements identified as low risk. With their focus on reducing the administrative burden, these agreements are subject to less scrutiny and attention than are other contribution agreements. Such a process could entail, for example, a federal organization periodically reassessing a representative sample of its low-risk recipients and reconfirming the risk ratings assigned. This assessment could inform the federal organization of the extent to which it appropriately applied a low-risk rating. At the same time, it could provide valuable information about how frequently risk ratings should be reassessed due to changes in factors such as the operating environment and stability of external organizations in a given industry or sector.

2.44 We found that the federal organizations we examined each had a process for some form of reassessment of risk ratings for multi-year agreements, although the processes in place were inconsistent and varied in rigour and depth of review. For example, one federal organization reassessed project risk ratings for each agreement every year, another did so only if there were amendments to the agreements, and yet another did so only if the project risks were being reassessed for other reasons.

2.45 We noted that guidance provided by the Secretariat supports reassessments, but does not guide federal organizations on whether and when risk ratings of agreements should be reassessed to ensure that they remain current. Without any specific guidance about the need for an internal challenge and review function for risk assessments, nor the need to have a formalized process for reassessment of risks for multi-year agreements, the ratings assigned to some agreements may be more appropriate than for others. This is important as these ratings affect the organizational controls used to manage grant and contribution programs.

2.46 Recommendation. The Treasury Board of Canada Secretariat should provide guidance to federal organizations on the need for a review and challenge function for initial risk assessments, as well as the need to periodically reassess the risk ratings of multi-year contribution agreements.

The Secretariat's response. Agreed. Deputy heads are responsible for, and have the flexibility to tailor, how they apply risk-based principles in the administration of their grant and contribution programs. As part of the Secretariat's five-year review of the Policy on Transfer Payments in 2013, and its provision of ongoing support to federal organizations on risk management of grants and contributions, the Secretariat will examine opportunities to strengthen its guidance on the need for deputy heads to review and confirm risk assessments throughout the life cycle of grants and contributions.

Federal organizations consult on program changes

2.47 The new Policy on Transfer Payments required federal organizations to engage applicants and recipients in efforts to bring about innovative, cost-effective improvements in grant and contribution programs. The goal of this engagement was to ensure that the programs would be accessible, understandable, and usable.

2.48 We found that all federal organizations we looked at had processes in place for regularly obtaining feedback from applicants and recipients. For example, prior to making significant program changes that would place greater priority on commercialization of technologies, Western Economic Diversification Canada held a series of consultations with interested parties in Western Canada. It held over 80 meetings in all four provinces it serves. At these meetings, the Department explained the rationale for its revised focus and how future budget allocations would work. Participants confirmed that the Department was on the right track and supported the budget allocation proposal.

2.49 Human Resources and Skills Development Canada regularly holds consultations with its stakeholders. For example, in 2011, it consulted with small- and medium-sized employers, industry associations, and others to identify opportunities to improve its ability to promote investment in literacy and essential skills. These consultations included roundtable discussions in large cities, interviews with stakeholders, and follow-up interviews to identify effective “models of practice” for literacy and integration of essential skills. Participants identified the need for better tools, a more user-friendly website, and more marketing and promotion efforts. As a result of these and other consultations, the Department is modifying its web-based tools to make them more user-friendly.

Federal organizations have begun to establish service standards

2.50 Service standards commit the government to provide well-understood and consistent levels of service to applicants and recipients. They state the level of performance that citizens can reasonably expect from federal organizations under normal circumstances. The new Policy on Transfer Payments requires federal organizations to establish service standards for all new and continued grant and contribution programs approved or renewed after 31 March 2010.

2.51 We found that Human Resources and Skills Development Canada and Western Economic Diversification Canada had established service standards. These standards include acknowledgement of application, timelines to provide funding decisions to applicants, and the time it takes to issue payments. Human Resources and Skills Development Canada began tracking its service standards in April 2010, while Western Economic Diversification Canada has been tracking its service standards since January 2007. This information is being used to help managers identify areas to focus increased efforts.

2.52 Other federal organizations are not as advanced in this regard. Natural Resources Canada has developed service standards and is in the process of determining which are most suitable and how best to use them. The Public Health Agency of Canada has developed service standards and is beginning to test them. The Canadian International Development Agency was in the process of determining what would constitute the most appropriate service standards, given the unique and multilateral process it uses for providing aid to recipient countries.

Conclusion

2.53 We concluded that, to date, the federal government has adequately implemented the 2008 Government Action Plan to Reform the Administration of Grant and Contribution Programs. It has fulfilled most of the commitments it made applicable at the time of the audit. It has put in place a new Policy on Transfer Payments that focuses monitoring and reporting requirements on the risks associated with the programs and recipients. Federal organizations have developed action plans and implemented concrete actions from those plans, and they are better coordinating their grant and contribution program activities.

2.54 The Treasury Board of Canada Secretariat (the Secretariat) is meeting the commitments it was assigned in the Policy on Transfer Payments. It has provided leadership and guidance to federal organizations to assist them in their efforts to implement the policy. It has also facilitated the development of new approaches to administer government grant and contribution programs.

2.55 The federal organizations we examined have implemented most of their obligations under the Policy on Transfer Payments. They have also consulted with applicant and recipient organizations in the redesign of their grant and contribution programs and are beginning to establish service standards. All five organizations have assessed the risks associated with their programs' agreements and have taken steps to adjust monitoring and reporting requirements in individual agreements based on these risks. However, the approach to risk assessment is not consistent across the organizations we examined. Those organizations do not have consistent processes in place to ensure that risk assessments are accurate and remain current. The Secretariat has provided little guidance on how and when federal organizations should reassess risk ratings.

2.56 Neither the Secretariat nor other federal organizations we audited have assessed the impact of their actions to date. As a result, they do not know the extent to which their actions have led to increased efficiency in their own programs or reduced the administrative burden for recipients. This information would support the government's planned five-year review of the Policy on Transfer Payments.

About the Audit

All of the audit work in this chapter was conducted in accordance with the standards for assurance engagements set by The Canadian Institute of Chartered Accountants. While the Office adopts these standards as the minimum requirement for our audits, we also draw upon the standards and practices of other disciplines.

Objectives

The overall objective of the audit was to determine if the government adequately implemented the 2008 Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs.

The sub-objectives were to determine whether

- the government has fulfilled the commitments made in the 2008 Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs;
- the Treasury Board of Canada Secretariat (as central agency) is meeting the policy requirements it was assigned, as articulated in the 2008 Policy on Transfer Payments; and
- selected federal organizations have implemented selected policy requirements in the 2008 Policy on Transfer Payments for selected programs.

Scope and approach

The audit assessed whether the federal government adequately met its commitments to improve the management of grants and contributions in response to the recommendations of the independent Blue Ribbon Panel on Grant and Contribution Programs.

We included the Treasury Board of Canada Secretariat in the audit scope because of its responsibilities for implementing the Government Action Plan in response to the Blue Ribbon Panel, and for guiding and monitoring implementation of the Policy on Transfer Payments.

We selected five federal organizations to assess the implementation of government commitments. We identified these organizations after considering the views of subject matter specialists, past audit coverage, and an analysis of grant and contribution expenditures. The federal organizations are

- Canadian International Development Agency (CIDA),
- Human Resources and Skills Development Canada (HRSDC),
- Natural Resources Canada (NRCan),
- Public Health Agency of Canada (PHAC), and
- Western Economic Diversification Canada (WD).

Two federal organizations, CIDA and HRSDC, were identified by the Treasury Board of Canada Secretariat as “vanguard” organizations in 2008 at the beginning of the reform process. Vanguard organizations started reforming their grant and contribution programs prior to the new 2008 Policy on Transfer Payments.

Note that the CIDA Bilateral Program, including the Tanzania program that we examined, was renewed only in April 2012 and therefore was not subject to all of the provisions of the Policy on Transfer Payments until April 2012. However, recognizing that CIDA was a vanguard organization and had various pilot initiatives in progress, we assessed the extent to which the program selected was already meeting the requirements of the Policy on Transfer Payments.

We assessed processes and practices followed by these federal organizations to implement their commitments under the Policy on Transfer Payments. We also obtained a sample of 38 grant and contribution agreements from selected programs that collectively possess the following characteristics:

- They include representation of major grant and contribution programs in vanguard organizations—CIDA and HRSDC.
- They represent programs from different sectors: international, social, environment, health, and economic.
- They represent multiple sizes of programs in terms of number of recipients.
- They represent multiple sizes of programs in terms of dollars spent per year.

We collected information through analysis of sample files, reports, and selected funding agreements. We conducted interviews with officials at the Centre of Expertise on Transfer Payment within the Secretariat and within selected entities. We also interviewed entity officials who are responsible for managing the selected programs.

Criteria

| Criteria | Sources |
|--|--|
| <p>To determine whether the government has fulfilled the commitments made in the 2008 Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs, we used the following criteria:</p> | |
| <p>The government has met the commitments made in the 2008 Action Plan stemming from the Blue Ribbon Panel, specifically by</p> <ul style="list-style-type: none"> • reforming the policies; • establishing departmental action plans and implementing changes to improve service delivery, increase efficiency, and share best practices; and • providing sustained leadership and ongoing support for consistent implementation of new and more streamlined approaches to the administration of grants and contributions. | <ul style="list-style-type: none"> • The Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs, Treasury Board of Canada Secretariat • From Red Tape to Clear Results, Independent Blue Ribbon Panel on Grant and Contribution Programs |

| Criteria | Sources |
|---|--|
| <p>To determine whether the government has fulfilled the commitments made in the 2008 Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs, we used the following criteria: (continued)</p> | |
| <p>The Treasury Board of Canada Secretariat is meeting the requirements of the 2008 Policy on Transfer Payments for grant and contribution program management, specifically in the following areas:</p> | <ul style="list-style-type: none"> • Policy on Transfer Payments, Treasury Board, 2008 • <i>Federal Accountability Act</i> |
| <ul style="list-style-type: none"> • Leadership and support. Promotes and facilitates collaboration among federal organizations for government-wide harmonization of grant and contribution programs, standardization of administration, and sharing of best practices. • Monitoring. Monitors federal organizations' compliance with this policy and its supporting directives, recommending corrective action to be taken in cases of non-compliance. • Review of policy. Establishes a framework to ensure timely review of this policy. | |
| <p>Federal organizations have implemented selected requirements in the 2008 Policy on Transfer Payments for selected programs, specifically with regard to the</p> <ul style="list-style-type: none"> • risk-based approach, • engagement of applicants and recipients, • service standards, • monitoring of federal organizations, and • control of contribution agreements. | <ul style="list-style-type: none"> • Policy on Transfer Payments, Treasury Board, 2008 • Directive on Transfer Payments, Treasury Board of Canada Secretariat • Guideline on the Directive on Transfer Payments, Treasury Board of Canada Secretariat |

Management reviewed and accepted the suitability of the criteria used in the audit.

Period covered by the audit

The audit covered the period from October 2011 to May 2012. Audit work for this chapter was completed on 17 July 2012.

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Appendix List of recommendations

The following is a list of recommendations found in Chapter 2. The number in front of the recommendation indicates the paragraph where it appears in the chapter. The numbers in parentheses indicate the paragraphs where the topic is discussed.

| Recommendation | Response |
|---|--|
| <p>Implementing the Government Action Plan</p> <p>2.26 The Treasury Board of Canada Secretariat should strengthen its process for gathering government-wide results-based information from federal organizations on the internal administrative impact of their activities in support of the Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs. It should also assess the impact to date on recipients' administrative burden associated with implementing the Government Action Plan. Results of this assessment should be made available publicly and be used in support of preparing the five-year review of the Policy on Transfer Payments. (2.22–2.25)</p> | <p>Agreed. In collaboration with federal organizations, the Secretariat will implement, in 2012 and 2013, a new results-based reporting tool to collect information on the impact, on recipients and departments, of the efforts to reform the administration and delivery of grant and contribution programs. Results of the whole-of-government assessment will be publicly available to coincide with the conclusion of the Secretariat's implementation of the Government Action Plan, and will be considered as part of the five-year review of the Policy on Transfer Payments.</p> |
| <p>Implementing policy reforms</p> <p>2.46 The Treasury Board of Canada Secretariat should provide guidance to federal organizations on the need for a review and challenge function for initial risk assessments, as well as the need to periodically reassess the risk ratings of multi-year contribution agreements. (2.27–2.45)</p> | <p>Agreed. Deputy heads are responsible for, and have the flexibility to tailor, how they apply risk-based principles in the administration of their grant and contribution programs. As part of the Secretariat's five-year review of the Policy on Transfer Payments in 2013, and its provision of ongoing support to federal organizations on risk management of grants and contributions, the Secretariat will examine opportunities to strengthen its guidance on the need for deputy heads to review and confirm risk assessments throughout the life cycle of grants and contributions.</p> |

Report of the Auditor General of Canada to the House of Commons

Matters of Special Importance

Main Points—Chapters 1 to 7

Appendices

Planning the Use of Professional Service Contractors

Grant and Contribution Program Reforms

Protecting Canadian Critical Infrastructure Against Cyber Threats

Transition of Ill and Injured Military Personnel to Civilian Life

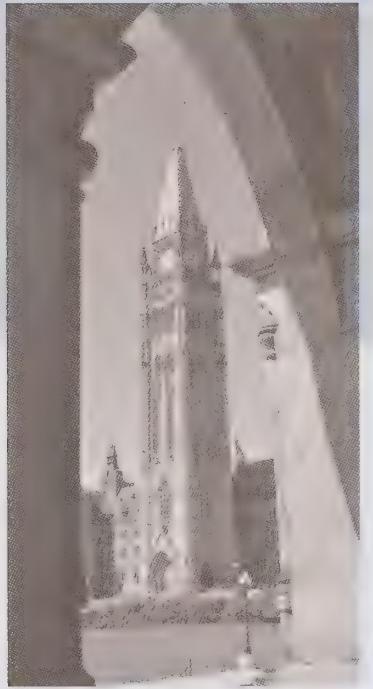
Real Property—National Defence

Transfer Payments to the Aerospace Sector—Industry Canada

Long-Term Fiscal Sustainability—Finance Canada

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Report of the Auditor General of Canada to the House of Commons

Protecting Canadian Critical Infrastructure Against Cyber Threats



Office of the Auditor General of Canada

fall 2012



Report of the Auditor General of Canada to the House of Commons

CHAPTERS

Protecting Canadian Critical Infrastructure Against Cyber Threats



Office of the Auditor General of Canada

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CHAPTER 3

Protecting Canadian Critical Infrastructure Against Cyber Threats



Performance audit reports

This report presents the results of a performance audit conducted by the Office of the Auditor General of Canada under the authority of the *Auditor General Act*.

A performance audit is an independent, objective, and systematic assessment of how well government is managing its activities, responsibilities, and resources. Audit topics are selected based on their significance. While the Office may comment on policy implementation in a performance audit, it does not comment on the merits of a policy.

Performance audits are planned, performed, and reported in accordance with professional auditing standards and Office policies. They are conducted by qualified auditors who

- establish audit objectives and criteria for the assessment of performance;
- gather the evidence necessary to assess performance against the criteria;
- report both positive and negative findings;
- conclude against the established audit objectives; and
- make recommendations for improvement when there are significant differences between criteria and assessed performance.

Performance audits contribute to a public service that is ethical and effective and a government that is accountable to Parliament and Canadians.

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Protecting Canadian Critical Infrastructure Against Cyber Threats

Main Points

What we examined

Critical infrastructure consists of physical and information technology assets, such as the electricity distribution networks, telecommunications networks, banking systems, manufacturing and transportation systems, as well as government information systems and services that support the continued and effective functioning of government. Elements of critical infrastructure can be stand-alone or interconnected and interdependent within and across provinces, territories, and international borders. Most of Canada's critical infrastructure is owned by the private sector or by municipal, provincial, or territorial governments, and much of it is connected to other systems.

Cyber threats to Canada's critical infrastructure refer to the risk of an electronic attack through the Internet. Such attacks can result in the unauthorized use, interruption, or destruction of electronic information or of the electronic and physical infrastructure used to process, communicate, or store that information.

Our audit examined whether selected federal departments and agencies are working with the provinces and territories and the private sector to protect Canada's critical infrastructure against cyber threats. This included examining leadership roles and responsibilities for securing key government information systems.

Audit work for this chapter was completed on 17 July 2012. More details on the conduct of the audit are in **About the Audit** at the end of this chapter.

Why it's important

Canada's public and private sectors depend on a secure, robust, and stable information infrastructure to conduct day-to-day operations. Computer-based systems, together with their Internet and network connections, form the backbone for much of Canada's critical infrastructure, including the energy, finance, telecommunications, and manufacturing sectors as well as government information systems. The smooth operation of critical infrastructure supports our way of life and Canada's economic, political, and social well-being.

Attacks on aspects of critical infrastructure of many nations, including Canada, have been reported. The government has stated that the frequency and severity of cyber threats are accelerating and it considers that protecting Canadians in cyberspace will be a constantly evolving challenge. The government has concerns that the cyber threat environment is evolving more rapidly than the government's ability to keep pace.

What we found

- Between 2001 and 2009, the government made limited progress in its efforts to lead and coordinate the protection of Canada's critical infrastructure from cyber threats as these threats were rapidly evolving. During this time, the government released several strategies and policies with recurring commitments and funding.
- Since 2010, with the announcement of the Cyber Security Strategy and of the National strategy and action plan for critical infrastructure, the government has made progress in securing its systems against cyber threats, in improving communications, and in building partnerships with owners and operators of critical infrastructure.
- Eleven years after the government said it would establish partnerships with other levels of government and with critical infrastructure owners and operators to help protect Canada's critical infrastructure, not all of the sector networks that facilitate these partnerships are fully established, and coverage is incomplete. This lack of progress limits Public Safety Canada's ability to communicate with critical infrastructure owners and operators.
- Seven years after the Canadian Cyber Incident Response Centre (CCIRC) was created to collect, analyze, and share cyber threat information among federal departments, provincial and territorial governments, and the private sector, many stakeholders are still unclear about the Centre's role and mandate. As a result, the CCIRC cannot fully monitor Canada's cyber threat environment, which hinders the Centre's ability to provide timely advice on defending against new cyber threats. Furthermore, the Centre is still not operating on a 24-hour-a-day, 7-day-a-week basis, as originally intended. This restriction on operating hours can delay the detection of emerging threats and the sharing of related information among stakeholders.

- The January 2011 intrusion on government systems identified weaknesses in protecting these systems. Incidents were not reported in a timely manner and cyber threat information was not properly shared with appropriate agencies. Also, good information technology (IT) security practices, such as how to store sensitive information, were not consistently followed. Lead security agencies are taking action by updating the government's IT Incident Management Plan to clarify the roles and responsibilities of lead security agencies and to address the need for timely reporting of incidents. The government has allocated more funds to bolster its capacity to detect cyber threats, and is working to increase awareness of best practices for IT security across the government.

The entities have responded. The entities agree with all of the recommendations. Their detailed responses follow the recommendations throughout the chapter.

Introduction

3.1 Canada's critical infrastructure consists of physical and information technology assets, such as the electricity distribution networks, telecommunications networks, banking systems, manufacturing and transportation systems, and government information systems. All of these assets and systems support the safety, security, and economic well-being of Canadians.

3.2 Elements of critical infrastructure are often interconnected and interdependent within and across provincial, territorial, and international borders. Protecting critical infrastructure from cyber threats is a responsibility that is shared among the Government of Canada, the provinces and territories, and the private sector.

3.3 Through the Internet, computer systems that control critical infrastructure can be subjected to a **cyber attack** from anywhere in the world using inexpensive hardware and software. Over time, hackers, criminal organizations, terrorists, and foreign states can quietly and methodically target a critical infrastructure's computer systems, attempt to defeat these systems' defences, and acquire their control. Once they achieve control, intruders can disrupt or destroy the systems or use them for their own purposes, such as stealing information. Attackers may also try to stay undetected within these computer systems for future exploitation.

3.4 Critical infrastructures in Canada and in other nations have been the target of cyber-related attacks for criminal, political, or other motives (Exhibit 3.1). Cyber attack tools and techniques have quickly evolved. The federal government has stated that the frequency and severity of cyber threats are growing and that protecting Canadians in cyberspace will be a constantly evolving challenge. Officials told us that the government has concerns that the cyber threat environment is evolving more rapidly than the government's ability to keep pace.

3.5 A cyber assault on key Estonian websites in 2007 illustrates the effects of cyber attacks on critical infrastructure. During a three-week period, websites of government ministries, service providers, banks, and news organizations were the target of a concerted attack that blocked access to users. The denial-of-service attack not only affected large entities, such as banks, media corporations, and government institutions, but also small and medium-sized businesses, all of which experienced disruptions to daily activities.

Cyber attack—[T]he unintentional or unauthorized access, use, manipulation, interruption or destruction (via electronic means) of electronic information and/or the electronic and physical infrastructure used to process, communicate and/or store that information.

Source: Government of Canada Cyber Security Strategy

Exhibit 3.1 US Government Accountability Office audits show that challenges remain in dealing with cyber threats

In 2011 and 2012, the US Government Accountability Office (GAO) reported that protecting the systems supporting the United States' critical infrastructure is a high risk for government. The GAO found that cyber-based threats to critical infrastructure and federal systems were evolving and growing. Over the past six years, the number of incidents reported by federal agencies increased by nearly 680 percent. Recently reported incidents include a sophisticated computer attack targeting a system used to operate industrial processes in critical sectors, including the energy and nuclear sectors, and another attack by hackers to access the personal information of hundreds of thousands of customers of a major bank.

The GAO found that despite recent actions taken, a number of significant challenges remain to enhancing the security of cyber-reliant critical infrastructures, such as strengthening public-private partnerships, particularly for information sharing, and improving the national capability for cyber warning and analysis.

Source: US Government Accountability Office reports

3.6 The Government of Canada plays an important role in protecting the nation's critical infrastructure from all hazards, including cyber threats. As the Prime Minister of the day stated in 2001, "The protection of Canada's critical infrastructure from the risks of failure or disruption is essential to assuring the health, safety, security and economic well-being of Canadians." The Prime Minister announced the creation of the Office of Critical Infrastructure Protection and Emergency Preparedness (OCIEP) to develop and implement a comprehensive approach to protecting Canada's critical infrastructure.

3.7 Since then, Public Safety Canada, which was created in 2003, has assumed the responsibilities of OCIEP.

Focus of the audit

3.8 In this audit, our objective was to determine whether selected federal departments and agencies are helping to secure Canada's critical infrastructure from cyber threats by leading and coordinating activities in partnership with provinces, territories, and the private sector. We also examined whether leadership roles and responsibilities for securing information systems that are important to the operation of the Government of Canada are clear and are being fulfilled as intended.

3.9 This audit focused on the prevention and preparedness efforts required to protect Canada's critical infrastructure against cyber threats. It did not examine response and recovery activities.

3.10 Legislation and policy require a number of federal departments and agencies to lead and coordinate federal efforts to help secure critical infrastructure and to work with provinces, territories, and

private sector owners of critical infrastructure where necessary. We included the activities of these departments and agencies in the audit:

- Canadian Security Intelligence Service,
- Communications Security Establishment Canada,
- Department of Finance Canada,
- Industry Canada,
- Department of Justice Canada,
- Natural Resources Canada,
- Privy Council Office,
- Public Safety Canada,
- Royal Canadian Mounted Police,
- Shared Services Canada, and
- Treasury Board of Canada Secretariat, including the Chief Information Officer Branch.

3.11 We did not examine matters of provincial or territorial jurisdiction, nor did we examine provincial and territorial or private sector protection efforts for critical infrastructure. We also did not examine any classified systems or new legislative authorities provided to law enforcement agencies to combat cyber crime.

3.12 The audit covered the period between the January 1999 release of The Report of the Special Senate Committee on Security and Intelligence and 31 May 2012. More details on the audit objectives, scope, approach, and criteria are in **About the Audit** at the end of this chapter.

Observations and Recommendations

Protecting critical infrastructure from cyber threats

3.13 In 1996, the federal government acknowledged that systems vital to operating Canada's critical infrastructure could be subject to cyber attacks and that the government had a role to play in protecting these systems from such attacks. In 1999, The Report of the Special Senate Committee on Security and Intelligence recommended that the government take action by reviewing its ability to assess and reduce infrastructure vulnerabilities and to prevent or respond to physical and cyber attacks.

3.14 In 2000, the Government of Canada established the Critical Infrastructure Protection Task Force to advise ministers on the role of

the federal government in protecting Canada's critical infrastructure. The task force found that the limited protection afforded to Canada's critical infrastructure, as well as its electronically interconnected and interdependent nature within and across provincial, territorial, and international borders, required a national strategy to strengthen security.

Situational awareness—Insight into one's environment and circumstances to understand how events and actions will affect business objectives, both now and in the near future. It requires understanding the relationships between critical services and information, the safeguards supporting information technology infrastructure and processes, and evolving threats.

3.15 The government is well positioned to provide critical infrastructure owners and operators with national and international situational awareness of the cyber threat environment because it has access to information sources, such as foreign intelligence sources, that are not available to other stakeholders. It can collect and share cyber threat information in a way that protects the source of the information and it can use established partnerships to inform all stakeholders quickly.

3.16 In response to the Critical Infrastructure Protection Task Force's concerns, the Government of Canada created the Office of Critical Infrastructure Protection and Emergency Preparedness (OCIEP) in 2001. The mandate of OCIEP was to develop and implement a comprehensive approach to protecting Canada's critical infrastructure by establishing partnerships and by monitoring and analyzing cyber attacks and threats against federal government systems.

3.17 In December 2003, the government announced that OCIEP would be integrated into the newly created Public Safety Canada to consolidate emergency response activities and to work with provinces, territories, and the private sector owners and operators of critical infrastructure. Exhibit 3.2 details the timeline of the federal government's commitments to protect Canada's critical infrastructure, including protection from cyber threats.

3.18 In the *Department of Public Safety and Emergency Preparedness Act* (2003), Public Safety Canada is responsible for exercising national leadership on public safety and emergency preparedness. But Public Safety Canada does not direct provinces, territories, critical infrastructure owners, or other federal departments on how to carry out their activities. Based on OCIEP's mandate, the National Security Policy, the National strategy and action plan for critical infrastructure, and Canada's Cyber Security Strategy, Public Safety Canada is to exercise its leadership and coordination role by providing unique support and services to critical infrastructure owners and operators that otherwise may not be available to them. These include

- building partnerships and providing a forum for advancing the timely sharing of cyber threat information among stakeholders;
- monitoring the international and national cyber threat environment to obtain timely and relevant warnings of cyber

security vulnerabilities and to analyze cyber threats to critical infrastructure stakeholders; and

- building critical infrastructure protection capacity through an enhanced policy framework, education and awareness, and research and development.

Exhibit 3.2 Commitments to protect Canada's critical infrastructure go back more than 11 years

| Year | Source | Federal government commitment |
|------|---|--|
| 2001 | OCIPEP mandate | <p>Provide national leadership to help ensure the protection of Canada's critical infrastructure, both its physical and cyber elements, by</p> <ul style="list-style-type: none"> • building partnerships and promoting dialogue among Canada's critical infrastructure owners and operators; • monitoring critical infrastructure around the clock; • building national capacity; and • securing government systems. |
| 2004 | National Security Policy | <p>To ensure that Canada is prepared for and can respond to current and future threats, including reducing Canada's vulnerability to cyber attacks and cyber accidents, the Government of Canada committed to</p> <ul style="list-style-type: none"> • building partnerships; • working with provinces, territories, and the private sector on national capabilities in critical infrastructure protection; • securing government systems by increasing capacity to predict and prevent cyber attacks against government systems; • modernizing the <i>Emergency Management Act</i> to include critical infrastructure protection and cyber security; • developing a critical infrastructure protection strategy; and • developing a national cyber security strategy. |
| 2005 | Review of the National Security Policy | <p>The Canadian Cyber Incident Response Centre (CCIRC) was announced with the mandate of</p> <ul style="list-style-type: none"> • serving as a national focal point for cyber security readiness and response; • dealing with threats and attacks to Canada's cyber critical infrastructure 24 hours a day, 7 days a week; and • building national capacity (by providing standards, best practices, awareness, and education). |
| 2010 | National strategy and action plan for critical infrastructure | <p>The strategy's goal is to enhance the resiliency of critical infrastructure in Canada by</p> <ul style="list-style-type: none"> • building partnerships; and • advancing the timely sharing and protection of information among partners. |
| 2010 | Canada's Cyber Security Strategy | <p>Canada plans to meet the cyber threat by</p> <ul style="list-style-type: none"> • securing government systems; • partnering to secure vital cyber systems outside the federal government; and • helping Canadians to be secure online. |

Funding of \$780 million was allocated for emergency management and other national security activities, including critical infrastructure protection

3.19 To determine how much funding had been allocated to cyber protection of critical infrastructure activities, we examined government approval documents and identified 13 federal departments and agencies that received funding approval between 2001 and 2011 in support of their activities. We noted that approvals identified four key areas:

- critical infrastructure protection of Government of Canada and private sector systems, and emergency management capacity building;
- addressing security priorities on intelligence and cyber security;
- enhancing cyber protection of Government of Canada information systems; and
- implementing Canada's Cyber Security Strategy.

3.20 We identified about \$780 million in funding approvals to these 13 departments and agencies where cyber security for critical infrastructure and government systems was one of the objectives. However, we found that these approvals included several objectives under the broad categories of emergency management and national security. The approved funding requests did not specify amounts for cyber protection activities. We then found that departmental documents supporting the requests for funding also did not specify how much funding was expected to go toward cyber protection activities. Therefore, we were unable to determine how much of the \$780 million was specifically allocated to activities for the protection of critical infrastructure from cyber threats. We also identified a further \$200 million in ongoing funding where cyber security for critical infrastructure was part of the approval, but we were not able to match funding to cyber protection activities.

3.21 Of the \$780 million, we did identify that about \$570 million was approved for Communications Security Establishment Canada (CSEC). We were informed by CSEC officials that, in line with the approvals, this funding was provided for more than just cyber protection activities; it also was intended to improve CSEC's overall program capacity, some of which could directly or indirectly support cyber protection of critical infrastructure. We asked officials at Public Safety Canada about funding to the other departments, but found that little information was available to show how much funding was directed by departments for their activities. Nevertheless,

Public Safety Canada officials informed us that about \$20.9 million of the remaining \$210 million was directed toward cyber protection for critical infrastructure between 2001 and 2011.

Since 2001, missing action plans have hindered progress

3.22 Action plans are important tools to guide the implementation of any initiative. We examined whether the government had action plans to guide its implementation of the commitments to protect Canada's critical infrastructure as outlined in Exhibit 3.2.

3.23 We asked Public Safety Canada for action plans that would provide more information on how funds for cyber security were to have been spent, what they were to achieve, and by when. The Department was not able to provide us with action plans, as none had been developed, with the exception of the National strategy and action plan for critical infrastructure.

3.24 The government has restated in several strategies and policies since 2001 its commitment to protecting Canada's critical infrastructure from cyber threats. However, while we noted that there has been progress in enhancing the policy frameworks, such as developing the Cyber Security Strategy and the National strategy and action plan for critical infrastructure, progress toward building partnerships and monitoring threats has been limited. In our opinion, the lack of action plans since the 2001 commitments for cyber security were announced has contributed to the overall lack of measurable progress. We noted that the 2010 Cyber Security Strategy does not yet have an action plan to guide its implementation. The lack of a plan makes it difficult to determine whether progress is on schedule and whether its objectives have been met.

3.25 Recommendation. Public Safety Canada should develop an interdepartmental action plan with deliverables and timelines for Canada's Cyber Security Strategy (2010) to guide the implementation of the strategy and measure progress.

The Department's response. Agreed. Public Safety will release an interdepartmental action plan. This action plan will be based on the implementation plan that was developed prior to the launch of the Cyber Security Strategy in October 2010. Since some of the activities in that plan were of a sensitive nature and dealt with issues related to national security, the plan was not publicly released. Public Safety Canada is currently leading the development of a horizontal performance measurement strategy to measure and report on the progress made against commitments in the implementation plan.

Partnering to protect critical infrastructure

3.26 Most of Canada's critical infrastructure is owned by the private sector or is managed through other levels of government. This mix of ownership and jurisdictions creates challenges in leading and coordinating stakeholders' efforts to protect Canada's critical infrastructure from cyber threats, for a number of reasons:

- Significant numbers of stakeholders are involved. Federal government departments, provinces, territories, the private sector, and international partners all need to agree on how to protect Canada's critical infrastructure.
- Critical infrastructure, such as the electricity distribution network, is geographically dispersed throughout North America, spanning both Canada and the United States, thereby requiring international cooperation.
- In some cases, stakeholders are reluctant to share information that is sensitive or of a competitive nature.

3.27 Through consultations in 2001, the Office of Critical Infrastructure Protection and Emergency Preparedness found that critical infrastructure owners and operators had suggested a collaborative approach for assuring the protection of critical infrastructure. The government therefore determined that building partnerships with all critical infrastructure owners and operators would be the best way to achieve the cooperation needed to coordinate efforts. The government has committed to building partnerships with critical infrastructure owners and operators consistently since then.

3.28 In 2003, as outlined in the National Critical Infrastructure Assurance Program Discussion Paper, the federal government acknowledged that dialogue with critical infrastructure owners and operators was needed to launch effective partnerships. This view was further supported in the 2004 Government of Canada Position Paper on a National Strategy for Critical Infrastructure Protection. Public Safety Canada was tasked with creating the partnerships needed to provide national direction and coordination of critical infrastructure protection.

3.29 Between 2004 and 2008, Public Safety Canada continued its work on developing these partnerships and monitoring the nature and extent of threats to critical infrastructure. In 2008, the Department produced Working Towards a National Strategy and Action Plan for Critical Infrastructure, in which it proposed strengthening the resiliency of Canada's critical infrastructure by creating partnerships with provinces, territories, and private sector owners of critical infrastructure.

3.30 In May 2010, the government released its National strategy and action plan for critical infrastructure. The strategy proposed that partnerships with provinces, territories, and private sector owners and operators be implemented through 10 sector networks. The federal government planned to have these sector networks in place by May 2011.

Building partnerships to protect critical infrastructure has been slow

3.31 We examined the progress the government has made since its initial commitment to build partnerships with the private sector, provinces, and territories.

3.32 At the time of our audit, 11 years after the Government of Canada first committed to using partnerships to strengthen Canada's critical infrastructure protection, we found uneven progress in establishing working sector networks. Based on Public Safety Canada's monitoring, we found that limited progress had been achieved and that the sector networks are at various stages of maturity. All 10 networks have **sector risk profiles** and lead departments identified, but 6 did not include representatives from all the industry groups that Public Safety Canada identified as key stakeholders. We also noted that while most have met, only 5 have included cyber security in their discussions.

3.33 Critical infrastructure sector networks are meant to be forums for discussions and information exchanges among sector-specific industry stakeholders and governments. Membership is voluntary. The National strategy and action plan for critical infrastructure explains that these sector networks are expected to identify and address interdependencies within and across sectors and to develop plans and programs that will protect critical infrastructure.

3.34 We found that the energy and utilities sector network, managed through Natural Resources Canada, meets regularly and has active participation from all stakeholders. We reviewed the network's stakeholder survey and found a high degree of satisfaction and commitment among members. In our opinion, this result shows that networks can work and can be a valuable forum for exchanging needed information to protect critical infrastructure.

3.35 We also found that the information and communication technology sector network has been established. This network was to represent several sub-sectors as defined in Public Safety Canada's Sector Risk Profile, which lists which industries should participate.

Sector risk profile—An overview developed by Public Safety Canada for each sector that contains a list of the sub-sectors that should be included in the sector network.

However, we found that the network includes only the telecommunications providers, which meet regularly. We asked Industry Canada, the lead federal department for the sector, and Public Safety Canada why other groups, such as radio and television broadcasters, global navigation, remote sensing, and identity management, were not included. The departments told us that the decision was taken to focus only on telecommunications and to expand coverage at a later date.

3.36 The government's approach to implementing its Cyber Security Strategy was to use sector networks with critical infrastructure owners and operators to build the partnerships needed to secure systems. However, since sector networks are only now starting to develop and are incomplete in coverage, one of the principal mechanisms for implementing the Cyber Security Strategy has been missing.

3.37 Recommendation. Public Safety Canada should ensure that all sector networks are fully established and operating as outlined in the National strategy and action plan for critical infrastructure so that they can be an effective tool in helping to secure critical infrastructure in order to deliver the objectives of Canada's Cyber Security Strategy.

The Department's response. Agreed. The sector networks provide a useful mechanism to deliver the private sector engagement objectives of Canada's Cyber Security Strategy, including sharing information on cyber threats and partnering with critical infrastructure sectors to conduct risk management activities. The Department will continue to work with lead federal departments and agencies to strengthen the sector networks, share information with sector stakeholders, including cyber threat information, and provide tools to support each sector's risk management efforts. Recognizing that each sector is unique and that representation is not expected to be uniform across each of the critical infrastructure sectors, Public Safety Canada will also provide guidance to lead federal departments and agencies on appropriate coverage for sector networks by December 2013.

Recent progress has been made to improve communications

3.38 Since the release of the Cyber Security Strategy and the National strategy and action plan for critical infrastructure, we found that there has been activity toward improving communication among stakeholders. For example:

- The National Cross Sector Forum was created to represent the 10 sector networks and has met twice since December 2010.

- A multi-industry cross sector forum has also met once, in April 2012, as an alternative to the sector networks that are not yet fully functioning.
- The Critical Infrastructure Gateway (a web-based critical infrastructure information-sharing portal) was launched in March 2012 and the Information Sharing Framework (mechanisms and processes to support information sharing among the critical infrastructure community and protect this information from inappropriate disclosure) was approved in December 2011.
- Federal, provincial, and territorial officials have met to discuss cyber issues.
- A memorandum of understanding for sharing cyber security information was signed with the Canadian Electricity Association in March 2012.

Monitoring cyber threats to critical infrastructure

3.39 Constant monitoring of cyber threats is necessary to help stakeholders reduce vulnerabilities and defend their systems. In 2003, the National Critical Infrastructure Assurance Program Discussion Paper proposed that the Government of Canada provide warnings, alerts, advisories, and relevant threat assessments to critical infrastructure owners and operators. Alerts, warnings, and threat assessments from government sources are important because they can provide owners and operators with knowledge and information that may not otherwise be available to them; that information helps them protect their assets from cyber threats.

3.40 In 2005, Public Safety Canada established the Canadian Cyber Incident Response Centre (CCIRC) as Canada's focal point for monitoring and providing advice on mitigating cyber threats. CCIRC is mandated to help owners and operators reduce risks to Canada's critical infrastructure from cyber threats by

- monitoring and analyzing cyber threats 24 hours a day, 7 days a week;
- providing security-related technical advice on information technology;
- providing standards, best practices, awareness, and education; and
- coordinating and supporting the Government of Canada's national response to cyber security incidents.

3.41 CCIRC's role was envisioned as an information hub for collecting relevant information from other federal departments, provincial and territorial governments, the private sector, and

foreign allies. CCIRC analyzes that information and distributes the analyses to stakeholders so they can use the information to better protect and defend their critical infrastructure.

Monitoring the cyber threat environment has not been complete or timely

3.42 We examined whether CCIRC was fulfilling its mandate to maintain situational awareness of the cyber threat environment in Canada. Our recommendation is found in paragraph 52.

3.43 Hours of operation. Since its creation, CCIRC has not operated 24 hours a day, 7 days a week to monitor and analyze cyber threats. At the time of the audit, the centre was staffed to operate from 8:00 a.m. to 4:00 p.m. (Ottawa time), five days a week. Cyber threats or attacks being reported to CCIRC after operating hours are received by the Government Operations Centre, which then pages a CCIRC employee who is on call at that time. That employee contacts the Government Operations Centre to determine the nature of the event and decide on the course of action.

3.44 As CCIRC is not operating around the clock, there is a risk that there will be a delay in the sharing of critical information linked to newly discovered vulnerabilities or active cyber events reported to CCIRC after operating hours. A restriction on operating hours means that CCIRC is not able to monitor the cyber threat environment 24 hours a day, as was envisioned in its mandate. Public Safety Canada officials told us that the Department is now working to extend CCIRC's coverage to 7 days a week, from 6:00 a.m. until 9:00 p.m. (Ottawa time), although there are no plans to go to a 24-hour-a-day operation. Based on our discussions with officials, it is our opinion that operating 24 hours a day, 7 days a week is important for the timely detection and notification of cyber threats, and for communicating with the computer emergency response teams of Canada's foreign allies, which operate in different time zones.

3.45 Timely information sharing. If infrastructure owners and operators communicate directly with other federal departments and agencies, CCIRC is left out of the discussion. When this happens, information is not always shared with CCIRC in a timely manner, which limits its situational awareness and reduces its ability to share that information as intended. Some private sector critical infrastructure owners and operators that we interviewed told us they were not sure whether cyber events should be reported to the Government of Canada and, if so, to which agency. In some cases, these owners and

operators speak directly with other federal agencies as part of their sector network. Others have said they were not aware of the existence of CCIRC or of the opportunity to share cyber threat information.

3.46 As a result, CCIRC is missing out on timely or complete cyber threat information from critical infrastructure owners and operators—information the centre needs to fully monitor Canada’s cyber threat environment. In our opinion, expanded hours of operation to improve access, as well as fully established sector networks, could improve stakeholders’ awareness about CCIRC.

3.47 As part of its mandate and under the Cyber Security Strategy, CCIRC was responsible for monitoring the cyber threat environment in Canada, including federal government systems, which allowed CCIRC to add the knowledge gained from its monitoring to its own alerts, warnings, and threat assessments. CCIRC relied on departments and agencies to keep it informed of cyber threats and attacks. This information could then be shared with all critical infrastructure owners and operators.

3.48 We noted that, during an incident where federal government systems were the target of hackers, CCIRC was not notified by the affected departments until more than one week after the intrusion was discovered, contrary to procedure.

3.49 In 2011, CCIRC transferred the responsibility for protecting government information systems to Communications Security Establishment Canada (CSEC). This transfer occurred because CSEC has the technical capacity and supporting mandate to protect government information systems from cyber threats. At the time of the transfer, it was agreed that CSEC would provide CCIRC with timely and complete information about identified threats to government systems. We found that CSEC has not been consistently providing CCIRC with timely and complete information gained from its monitoring of government systems. We asked officials from the two agencies what kept CSEC from sharing this information. CSEC told us it was concerned about sharing information because of the sensitive nature of the information it collects, such as classification levels or the sensitivities of client departments. This issue was to be resolved by the end of August 2011, but had not yet been resolved at the time of the audit. CSEC and CCIRC have agreed to resolve this issue by 30 November 2012 and have placed a CCIRC employee on a trial basis within CSEC to facilitate more frequent and secure information sharing.

3.50 Technical advice. As part of its mandate, CCIRC provides technical advice on defending against new cyber threats by maintaining an up-to-date awareness of the national and international cyber threat environment. This advice aims to help critical infrastructure owners and operators protect their systems from emerging sophisticated cyber threats. However, CCIRC's difficulties in collecting timely and complete cyber threat information reduce its ability to provide such advice promptly.

3.51 Education, awareness, and standards. We found that since its creation in 2005, CCIRC's efforts have been dedicated to analyzing the cyber threat environment and providing alerts and warnings to its stakeholders. It has been progressing slowly in two additional areas of its mandate: providing education and awareness of cyber threats and standards. Now, with the launch of the Cyber Security Strategy in 2010, Public Safety Canada has transferred these responsibilities from CCIRC to another section within its department.

3.52 Recommendation. Public Safety Canada should increase the Canadian Cyber Incident Response Centre's ability to maintain situational awareness of cyber threats to Canada's critical infrastructure and to increase the Centre's ability to communicate this information to critical infrastructure owners and operators.

The Department's response. Agreed. To enhance support for critical infrastructure and other partners, Public Safety Canada is augmenting CCIRC's operational capacity and capabilities, strengthening its policies and processes, and improving its information-sharing partnerships.

In 2012, the government allocated an additional \$13 million over five years to extend CCIRC's operational hours to 15 hours a day, 7 days a week. CCIRC's capabilities have been bolstered through the acquisition of a world-class malware analysis laboratory from the Communications Research Centre and the deployment of an industrial control systems test bed.

CCIRC's mandate has been updated to provide greater clarity to internal and external partners. Standard procedures and policies are being updated where necessary to support the expansion of CCIRC's operations, ensuring that CCIRC provides value-added services that are efficient, effective, and consistent.

Finally, CCIRC is improving information sharing with the introduction of the CCIRC Community Portal, a secure environment for collaboration, and the creation of formal information-sharing agreements with partners in the critical infrastructure; the first such agreement has recently been signed. Further, an incident response pilot has been launched with a number of partners, the lessons from which will greatly improve both response capability and cyber security readiness for all partners.

Protecting government information systems

3.53 In the National Security Policy (2004) and Canada's Cyber Security Strategy (2010), the government stated its commitment to better protect its information systems from cyber attacks. These systems include, for example, the networks where the government stores sensitive information during its daily operations and the networks that ensure that paycheques and employment insurance benefits are distributed on time. The security of government systems is necessary for the continued delivery of services upon which Canadians rely and for the continued and effective functioning of government.

3.54 To better protect its systems and improve the timely sharing of cyber threat information between departments, the government set out three objectives:

- strengthen the security of government systems,
- clarify roles and responsibilities for protecting government systems, and
- enhance awareness of information technology (IT) security in government departments.

Government information systems have been vulnerable to intrusion

3.55 We examined the government's progress in meeting these three objectives to protect its information systems, recognizing the rapidly evolving cyber threats. We found that since 2001, there has been limited progress on achieving these objectives, although there has been more progress recently to protect government information systems.

3.56 System security. The intrusion into government systems in January 2011 showed existing weaknesses in protecting these systems (Exhibit 3.3). Since that time, the government has taken additional steps to secure its systems. Communications Security Establishment Canada (CSEC) officials told us that the January 2011 incident would not have been detected without the enhancements that CSEC had made to its monitoring and that these enhancements have increased CSEC's success in stopping subsequent attempted attacks.

3.57 In 2010, in support of the Cyber Security Strategy, the government committed \$90 million toward achieving the strategy's objectives. It began phasing in this funding over the next five years, to be followed by recurring amounts of \$18 million each year. That same year, lead security agencies assessed the security risks to government systems to obtain funding to implement the Cyber Security Strategy.

3.58 The lessons learned exercise that was done after the January 2011 intrusion revealed ongoing vulnerabilities to government systems. As a result, new funding was approved in April 2012 to bolster the capacity of Public Safety Canada, CSEC, the Treasury Board of Canada Secretariat, and Shared Services Canada to detect cyber threats and enhance the government's ability to protect its systems. About \$31 million was allocated to these four departments for the 2012–13 fiscal year to provide additional resources to support the implementation of the Cyber Security Strategy.

3.59 Roles and responsibilities. The Policy on Government Security states that all deputy heads of federal departments must manage security activities so that information, assets, and services are safeguarded. However, the large number of departments and agencies involved has created challenges in sharing threat information and coordinating actions. Several departments and agencies—called lead

Exhibit 3.3 Government of Canada information systems were the target of an intrusion

In January 2011, departments of the federal government were the target of a cyber incident of significant scope. The intrusion was aimed at gaining access to and control of information systems, and extracting sensitive information contained within those systems.

As soon as the intrusion was detected, mitigation measures were taken to prevent any further damage, such as blocking staff access to the Internet. Affected departments deployed resources in response to the intrusion, resulting in several million dollars in IT equipment and urgent IT security enhancements, overtime, and lost productivity. Full employee access to the Internet was restored only in September 2011.

The intrusion also attracted national and international media attention, raising questions about the government's ability to protect sensitive government information.

security agencies—have been tasked under the policy to lead and coordinate activities and deliver services to assist in the shared protection of government systems. Exhibit 3.4 highlights these responsibilities. Under the leadership of the Treasury Board of Canada Secretariat, these responsibilities have been further defined and explained in the government's IT Incident Management Plan.

3.60 We found that the IT Incident Management Plan, which was released in 2009 after the Policy on Government Security was revised, contained aspects that did not comply with the policy. For example, departmental roles as described in the policy were different from the descriptions in the Incident Management Plan. The review of the events in January 2011 noted that because of this confusion, information about the cyber threat had not been shared quickly enough with appropriate departments.

3.61 The IT Incident Management Plan was updated in May 2012. This updated version clarifies roles and responsibilities of lead security agencies and addresses the need for timely reporting of incidents.

Exhibit 3.4 Many lead security agencies are involved in protecting government systems from cyber threats

| Agency | Responsibilities |
|--|---|
| Privy Council Office | Advising and supporting the Prime Minister and Cabinet on national security matters, coordinating the related activities of departments and agencies, and providing government-wide policy direction on national security and intelligence priorities |
| Treasury Board of Canada Secretariat | Setting government-wide direction, establishing priorities, and defining and formalizing IT security requirements for departments of the Government of Canada |
| Public Safety Canada | Coordinating activities related to IT incidents affecting the Government of Canada and monitoring IT threats to services to Canadians or government operations |
| Communications Security Establishment Canada | Leading and coordinating departmental activities to help ensure the protection of IT systems of importance |
| Public Works and Government Services Canada | Delivering IT security services, such as ensuring the confidentiality, integrity, and availability of common IT services provided to departments |
| Canadian Security Intelligence Service | Providing intelligence reports and assessments relating to IT security to help ensure the protection of the Government of Canada's critical services and systems |
| Royal Canadian Mounted Police | Providing services related to law enforcement and investigations including computer forensics and cyber crime |

Source: Adapted from the Policy on Government Security, 2009

Treasury Board of Canada Secretariat officials told us that, in their view, this revised plan better reflects more recent practices and structural changes within the government, such as the creation of Shared Services Canada.

3.62 Awareness of IT security. Lessons learned from the January 2011 intrusion also showed that sensitive information was being stored on government systems that did not meet appropriate information technology security safeguards. As a result, some of this sensitive information that was not appropriately protected against unauthorized access was vulnerable to compromise. Treasury Board of Canada Secretariat officials told us that a renewed emphasis on increasing awareness of best practices for IT security is now being implemented across the government.

The Policy on Government Security does not reflect current roles and responsibilities for information technology security

3.63 Shared Services Canada (SSC) is a federal department established in August 2011. In a presentation to the Standing Committee on Government Operations and Estimates in December 2011, the Minister responsible said that “Shared Services Canada was established earlier this year to reduce duplication in Government of Canada information technology, or IT, infrastructure services, to modernize the way we deliver services to Canadians, and to improve the security of federal IT infrastructure.”

3.64 We examined whether SSC’s leadership and coordination roles and responsibilities in protecting the Government of Canada’s information technology assets and systems have been defined and implemented.

3.65 SSC provides IT security for email systems, data centres, and electronic networks for 43 departments. As part of the government’s revised IT Incident Management Plan, SSC is tasked with IT security roles and responsibilities covering other departments. We found that since SSC was created after the release of the Policy on Government Security, SSC is not referenced as a lead security agency within that policy. The discrepancy between the revised IT Incident Management Plan and the Policy on Government Security could create confusion about the IT security role that SSC is expected to play under the IT Incident Management Plan and other government policies.

3.66 Government officials told us that consolidating the government’s IT services under SSC is a unique opportunity to develop a new conceptual design for the implementation of information technology in

the federal government that would embed security at its core. At a meeting of the Standing Committee on Government Operations and Estimates in December 2011, the Minister responsible for SSC said that “The consolidation of services and assets will strengthen our efforts to ensure that government IT infrastructure is reliable and secure.” This consolidation aims to improve security by improving control of access. The federal government expects this consolidation to be achieved by 2020.

3.67 Recommendation. Treasury Board of Canada Secretariat, in cooperation with Shared Services Canada, should update relevant policies and plans to reflect the new information technology security roles and responsibilities of Shared Services Canada.

The Department’s response. Agreed. Treasury Board Secretariat has revised the Government of Canada (GC) Information Technology (IT) Incident Management Plan, which defines the roles and responsibilities of Shared Services Canada (SSC) with respect to incident management. The GC IT Incident Management Plan was approved by the Chief Information Officer (CIO) of Canada in May 2012. Additionally, the Secretariat is updating the Policy on Government Security to reflect the role of SSC as one of the lead federal IT security agencies and to define its associated IT security roles and responsibilities. The updated policy is expected to be published in 2013.

Conclusion

3.68 Since 2001, the Government of Canada has made commitments to address the cyber threats to Canada’s critical infrastructure. Despite several past strategies and funding, we found that progress in achieving these commitments has been slow. Since 2010, with the announcement of Canada’s Cyber Security Strategy and of the National strategy and action plan for critical infrastructure, we found that the government has made progress in securing its systems against cyber threats and in improving communications and building some partnerships with owners and operators of critical infrastructure.

3.69 The government determined in 2001 that through partnerships with critical infrastructure owners and operators, it could help to protect Canada’s critical infrastructure by sharing information and providing technical support. These partnerships were to be set up by organizing 10 sector networks. However, the government has made little progress in building these partnerships through the use of the sector networks. This lack of progress restricts one of Public Safety Canada’s principal

mechanisms for communicating with critical infrastructure owners and operators as outlined in the Cyber Security Strategy.

3.70 The Government of Canada created the Canadian Cyber Incident Response Centre (CCIRC) in 2005 to be the focal point for monitoring systems and providing advice on mitigating cyber threats to critical infrastructure. The Centre was to operate 24 hours a day, 7 days a week, and was to direct the national response to cyber security incidents. After seven years of existence, CCIRC still does not monitor cyber threats to critical infrastructure full time. Not being able to operate at all times reduces CCIRC's ability to gain a complete situational awareness of the national and international cyber threat environment. The limited hours of operation also hamper CCIRC's ability to provide timely and relevant information and analyses to critical infrastructure stakeholders. A lack of timely and relevant information and analyses affects the ability of critical infrastructure owners and operators to react to cyber attacks that may cause disruptions.

3.71 The lessons learned exercise that was done after the January 2011 intrusion on government systems reported that the systems were vulnerable. Despite the Government of Canada's commitments and investments in system security, which date back to 2001, cyber incidents were not reported in a timely manner and cyber threat information was not properly shared with appropriate departments. Also, good IT security practices were not consistently followed. Lead security agencies have begun to take action by updating the government's IT Incident Management Plan. The government has allocated more funds to bolster its capacity to detect cyber threats and is renewing its emphasis on increasing employees' awareness of IT security best practices.

3.72 Since 2001, we found that selected departments and agencies of the federal government have made limited progress in leading and coordinating activities, with partners, to secure Canada's critical infrastructure from cyber threats. Since 2010, with the release of the Cyber Security Strategy and the National strategy and action plan for critical infrastructure, there have been several accomplishments on the part of government to improve communications and build partnerships, and to enhance the monitoring of government systems.

About the Audit

All of the audit work in this chapter was conducted in accordance with the standards for assurance engagements set by The Canadian Institute of Chartered Accountants. While the Office adopts these standards as the minimum requirement for our audits, we also draw upon the standards and practices of other disciplines.

Objectives

The objective of our audit was to determine whether selected departments and agencies of the federal government are leading and coordinating activities, with partners, to secure Canada's critical infrastructure from cyber threats.

Scope and approach

Our audit covered the planning, management, and delivery of Public Safety Canada's responsibilities to lead the efforts of federal entities to protect the Government of Canada's critical infrastructure from cyber threats, and to provide leadership and coordinate federal efforts with those of the provinces and territories as well as private sector owners of critical infrastructure. It focused primarily on preventive and preparedness efforts required to protect Canada's critical infrastructure against cyber threats. We also looked at how Public Safety Canada is increasing awareness of cyber threats and promoting safe cyber security practices.

The audit team interviewed staff, mostly senior management and analysts, from Public Safety Canada, Communications Security Establishment Canada, and officials from the Chief Information Officer Branch. Other personnel interviewed included representatives from Shared Services Canada and the Canadian Security Intelligence Service.

Specific audit questions were also directed to the Privy Council Office for its role in providing strategic guidance; the Department of Justice for its role in providing legal advice and opinions in supporting elements pertaining to threat-based information sharing, particularly sensitive information, between federal departments and agencies and with other stakeholders; and the Royal Canadian Mounted Police for its supporting role in collecting and acting upon information on cyber incidents related to critical infrastructure.

Finally, we carried out interviews at Industry Canada, Natural Resources Canada, the Department of Finance and with private sector owners and operators of critical infrastructure assets and systems.

The audit did not examine matters of provincial or territorial jurisdiction, or provincial and territorial or private sector critical infrastructure protection efforts. It did not examine any classified systems or new legislative authorities provided to law enforcement agencies to combat cyber crime.

Criteria

| Criteria | Sources |
|---|---|
| <p>To determine whether selected departments and agencies are leading and coordinating federal government activities to secure Canada's critical infrastructure against cyber threats, in partnership with provinces, territories, the private sector, and selected international partners, we used the following criteria:</p> | |
| <p>Selected departments and agencies are leading federal government activities with partners to secure Canada's critical infrastructure from cyber threats.</p> | <ul style="list-style-type: none"> • <i>Emergency Management Act</i> • <i>Department of Public Safety and Emergency Preparedness Act</i> • Canada's Cyber Security Strategy, Public Safety Canada • Policy on Government Security, Treasury Board, 2009 • National strategy and action plan for critical infrastructure, Public Safety Canada • National Security Policy: Securing an Open Society, Public Safety Canada |
| <p>Selected departments and agencies are coordinating the activities of partners in securing Canada's critical infrastructure from cyber threats.</p> | |
| <p>To determine whether leadership and coordination roles and responsibilities for securing the Government of Canada's critical infrastructure against cyber threats are being exercised as defined, we used the following criteria:</p> | |
| <p>The leadership role in securing the Government of Canada's critical infrastructure against cyber threats is being exercised as defined.</p> | <ul style="list-style-type: none"> • <i>Department of Public Safety and Emergency Preparedness Act</i> • <i>Emergency Management Act</i> • <i>Financial Administration Act</i> • Policy on Government Security, Treasury Board, 2009 • National strategy and action plan for critical infrastructure, Public Safety Canada • Canada's Cyber Security Strategy, Public Safety Canada |
| <p>Activities to secure the government's critical infrastructure against cyber threats are being coordinated as defined.</p> | <ul style="list-style-type: none"> • <i>Department of Public Safety and Emergency Preparedness Act</i> • <i>Emergency Management Act</i> • <i>Financial Administration Act</i> • <i>National Defence Act</i> • National Security Policy, Public Safety Canada • Policy on Government Security, Treasury Board, 2009 • Federal Policy for Emergency Management, Public Safety Canada • Policy on Management, Resources and Results Structures, Treasury Board • National strategy and action plan for critical infrastructure, Public Safety Canada • Canada's Cyber Security Strategy, Public Safety Canada |
| <p>To determine whether Public Safety Canada is helping to increase the awareness of Canadians against cyber threats, we used the following criteria:</p> | |
| <p>Public Safety Canada is promoting an increased awareness of cyber crimes and the use of safe cyber security practices.</p> | <ul style="list-style-type: none"> • <i>Emergency Management Act</i> • Policy on Government Security, Treasury Board, 2009 • Canada's Cyber Security Strategy, Public Safety Canada |

Management reviewed and accepted the suitability of the criteria used in the audit.

Period covered by the audit

The audit covered the period between the January 1999 release of The Report of the Special Senate Committee on Security and Intelligence and 31 May 2012. Audit work for this chapter was completed on 17 July 2012.

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Appendix List of recommendations

The following is a list of recommendations found in Chapter 3. The number in front of the recommendation indicates the paragraph where it appears in the chapter. The numbers in parentheses indicate the paragraphs where the topic is discussed.

| Recommendation | Response |
|--|---|
| <p>Protecting critical infrastructure from cyber threats</p> <p>3.25 Public Safety Canada should develop an interdepartmental action plan with deliverables and timelines for Canada's Cyber Security Strategy (2010) to guide the implementation of the strategy and measure progress. (3.22–3.24)</p> | <p>Agreed. Public Safety will release an interdepartmental action plan. This action plan will be based on the implementation plan that was developed prior to the launch of the Cyber Security Strategy in October 2010. Since some of the activities in that plan were of a sensitive nature and dealt with issues related to national security, the plan was not publicly released. Public Safety Canada is currently leading the development of a horizontal performance measurement strategy to measure and report on the progress made against commitments in the implementation plan.</p> |
| <p>Partnering to protect critical infrastructure</p> <p>3.37 Public Safety Canada should ensure that all sector networks are fully established and operating as outlined in the National strategy and action plan for critical infrastructure so that they can be an effective tool in helping to secure critical infrastructure in order to deliver the objectives of Canada's Cyber Security Strategy. (3.31–3.36)</p> | <p>Agreed. The sector networks provide a useful mechanism to deliver the private sector engagement objectives of Canada's Cyber Security Strategy, including sharing information on cyber threats and partnering with critical infrastructure sectors to conduct risk management activities. The Department will continue to work with lead federal departments and agencies to strengthen the sector networks, share information with sector stakeholders, including cyber threat information, and provide tools to support each sector's risk management efforts. Recognizing that each sector is unique and that representation is not expected to be uniform across each of the critical infrastructure sectors, Public Safety Canada will also provide guidance to lead federal departments and agencies on appropriate coverage for sector networks by December 2013.</p> |

Recommendation**Response****Monitoring cyber threats to critical infrastructure**

3.52 Public Safety Canada should increase the Canadian Cyber Incident Response Centre's ability to maintain situational awareness of cyber threats to Canada's critical infrastructure and to increase the Centre's ability to communicate this information to critical infrastructure owners and operators. (3.39–3.51)

Agreed. To enhance support for critical infrastructure and other partners, Public Safety Canada is augmenting CCIRC's operational capacity and capabilities, strengthening its policies and processes, and improving its information-sharing partnerships.

In 2012, the government allocated an additional \$13 million over five years to extend CCIRC's operational hours to 15 hours a day, 7 days a week. CCIRC's capabilities have been bolstered through the acquisition of a world-class malware analysis laboratory from the Communications Research Centre and the deployment of an industrial control systems test bed.

CCIRC's mandate has been updated to provide greater clarity to internal and external partners. Standard procedures and policies are being updated where necessary to support the expansion of CCIRC's operations, ensuring that CCIRC provides value-added services that are efficient, effective, and consistent.

Finally, CCIRC is improving information sharing with the introduction of the CCIRC Community Portal, a secure environment for collaboration, and the creation of formal information-sharing agreements with partners in the critical infrastructure; the first such agreement has recently been signed. Further, an incident response pilot has been launched with a number of partners, the lessons from which will greatly improve both response capability and cyber security readiness for all partners.

Protecting government information systems

3.67 Treasury Board of Canada Secretariat, in cooperation with Shared Services Canada, should update relevant policies and plans to reflect the new information technology security roles and responsibilities of Shared Services Canada. (3.63–3.66)

Agreed. Treasury Board Secretariat has revised the Government of Canada (GC) Information Technology (IT) Incident Management Plan, which defines the roles and responsibilities of Shared Services Canada (SSC) with respect to incident management. The GC IT Incident Management Plan was approved by the Chief Information Officer (CIO) of Canada in May 2012. Additionally, the Secretariat is updating the Policy on Government Security to reflect the role of SSC as one of the lead federal IT security agencies and to define its associated IT security roles and responsibilities. The updated policy is expected to be published in 2013.

Report of the Auditor General of Canada to the House of Commons

Matters of Special Importance

Main Points—Chapters 1 to 7

Appendices

Planning the Use of Professional Service Contractors

Grant and Contribution Program Reforms

Protecting Canadian Critical Infrastructure Against Cyber Threats

Transition of Ill and Injured Military Personnel to Civilian Life

Real Property—National Defence

Transfer Payments to the Aerospace Sector—Industry Canada

Long-Term Fiscal Sustainability—Finance Canada

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Report of the Auditor General of Canada to the House of Commons

Transition of Ill and Injured Military Personnel to Civilian Life



Office of the Auditor General of Canada



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Transition of Ill and Injured Military Personnel to Civilian Life



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CHAPTER 4

Transition of Ill and Injured Military Personnel to Civilian Life



Performance audit reports

This report presents the results of a performance audit conducted by the Office of the Auditor General of Canada under the authority of the *Auditor General Act*.

A performance audit is an independent, objective, and systematic assessment of how well government is managing its activities, responsibilities, and resources. Audit topics are selected based on their significance. While the Office may comment on policy implementation in a performance audit, it does not comment on the merits of a policy.

Performance audits are planned, performed, and reported in accordance with professional auditing standards and Office policies. They are conducted by qualified auditors who

- establish audit objectives and criteria for the assessment of performance;
- gather the evidence necessary to assess performance against the criteria;
- report both positive and negative findings;
- conclude against the established audit objectives; and
- make recommendations for improvement when there are significant differences between criteria and assessed performance.

Performance audits contribute to a public service that is ethical and effective and a government that is accountable to Parliament and Canadians.

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Transition of Ill and Injured Military Personnel to Civilian Life

Main Points

- What we examined** From 2006 to 2011, 8,026 Canadian Forces members were released from the military because of an injury or illness that ended their military career. Ill and injured members and veterans of the Canadian Forces have access to a variety of services, programs, and financial benefits to support their transition from military to civilian life.
- Support services and benefits, including those available under the New Veterans Charter, are provided, coordinated, and managed primarily by the Department of National Defence and the Canadian Forces, and Veterans Affairs Canada.
- Our audit looked at selected services and benefits provided to support eligible Canadian Forces members and veterans in their transition to civilian life. We examined how the Department of National Defence and the Canadian Forces, and Veterans Affairs Canada manage those services and benefits.
- We did not look at whether Canadian Forces members and veterans have received all benefits and services for which they were eligible. Neither did we examine the fairness of departmental services and benefits available, or the quality of medical treatment and care provided.
- Audit work for this chapter was completed on 17 July 2012. More details on the conduct of the audit are in **About the Audit** at the end of the chapter.
- Why it's important** Ill and injured members of the Canadian Forces and their families may need support in making the transition to civilian life and in coping with their illnesses and injuries. Others who have left the military may develop physical and/or mental health problems over time that are associated with their military service and become eligible for support. Research shows that early detection and appropriate treatment of illness and injuries can have a critical impact on the success of this support, which amounted to about \$500 million in the 2010–11 fiscal year.

How well National Defence and the Canadian Forces, and Veterans Affairs Canada coordinate and manage this support affects the quality of the transition to civilian life that ill and injured Canadian Forces members and veterans are able to make.

What we found

- Canadian Forces members and veterans, as well as departmental staff responsible for assessing eligibility and managing the delivery of services and benefits, find the transition process complex, lengthy, and challenging to navigate. Although National Defence and the Canadian Forces, and Veterans Affairs Canada recognize the challenges and have been working independently and jointly on solutions, it remains difficult to access services and benefits in a timely manner. Reasons include the complexity of eligibility criteria, lack of clear information on support available, the amount of paperwork involved, and case management services that require further improvement.
- Both departments have difficulties in communicating and meeting service delivery standards and requirements, particularly as they relate to assessments and case management services. The result may be that Forces members and veterans do not receive benefits and services to which they are entitled, or do not receive them in a timely manner.
- An overarching governance framework has been established to coordinate, harmonize, and communicate the various programs, services, and benefits available to ill and injured Forces members and veterans. However, it does not specify the authority, responsibility, and accountability of the joint steering committee—the key coordinating mechanism meant to help manage the transition, reintegration, and continuity of support to Forces members and veterans. In addition, measurable objectives and specific timelines have not been established for all joint priorities approved by the committee. The existence of similar income support and vocational rehabilitation programs within each department continues to create confusion and difficulties for veterans and program staff alike.

The departments have responded. The departments agree with all of the recommendations. Their detailed responses follow the recommendations throughout the chapter.

Introduction

4.1 The Government of Canada has made a commitment to provide care to ill and injured Canadian Forces members and veterans.

Through a variety of services, benefits, and programs (Exhibit 4.1), two federal departments have primary responsibility for fulfilling this commitment: National Defence and the Canadian Forces, and Veterans Affairs Canada.

4.2 The legislative mandate of National Defence and the Canadian Forces provides for comprehensive medical and dental services for Forces members until their release. (For reservists, the level of care is dependent on their employment status.) Ill and injured Forces members have access to additional support services, programs, and financial benefits. These include vocational rehabilitation and long-term disability benefits through the Service Income Security Insurance Plan (SISIP), as well as support intended to help navigate the administrative requirements and access benefits and services both before and after release.

4.3 The *Department of Veterans Affairs Act* mandates the Minister of Veterans Affairs with “the care, treatment or re-establishment in civilian life of any person who served in the Canadian Forces” and “the care of the dependants or survivors.” Veterans Affairs’ responsibility for eligible veterans’ re-establishment in civilian life begins after their release from the Forces, although planning to support the transition is to begin before release.

4.4 Veterans Affairs fulfills its responsibilities through a set of programs, benefits, and services under the *Canadian Forces Members and Veterans Re-establishment and Compensation Act* (commonly referred to as the New Veterans Charter), the *Pension Act*, and the *Department of Veterans Affairs Act*.

The transition to civilian life

4.5 According to the Canadian Forces, illnesses and injuries are identified through screenings on initial enrolment in the Forces, post-deployment, and release, as well as through self-reporting and periodic medical assessments. A Forces member in the process of being released for medical reasons should be assigned a Canadian Forces case manager, who is responsible for coordinating and monitoring a case plan aimed at addressing the member’s medical, psycho-social, and vocational needs.

Exhibit 4.1 Support for ill and injured military personnel offered by the Department of National Defence and the Canadian Forces, and Veterans Affairs Canada

| Support offered by the Department of National Defence and the Canadian Forces (DND/CF) | Available to Forces members (pre-release) | Available to veterans (post-release) |
|--|---|--------------------------------------|
| CF Case Management | ✓ | |
| Comprehensive Health Care | ✓ | |
| Operational Trauma and Stress Support Centres | ✓ | |
| Operational Stress Injury Social Support | ✓ | ✓ |
| Military Family Resource Centre | ✓ | |
| CF Family Peer Support Network | ✓ | ✓ |
| Chaplaincy services | ✓ | |
| Soldier On program | ✓ | |
| Injured Soldier Network | ✓ | |
| Shoulder 2 Shoulder Program | ✓ | ✓ |
| CF Member Assistance Program | ✓ | |
| CF Accidental Dismemberment Insurance Plan (SISIP) | ✓ | |
| Education Reimbursement | ✓ | |
| Skills Completion Program | ✓ | |
| Second Career Assistance Network | ✓ | |
| Return to Work Program | ✓ | |
| Joint Personnel Support Units / Integrated Personnel Support Centres | ✓ | ✓ |
| Transition Assistance Program | ✓ | ✓ |
| SISIP Financial Services, Vocational Rehabilitation Program | ✓ | ✓ |
| SISIP Financial Services, Long-Term Disability | | ✓ |
| Support offered by Veterans Affairs Canada (VAC) | | |
| VAC Case Management | ✓ | ✓ |
| Treatment benefits for awarded condition* (if not provided by CF) | ✓ | |
| Treatment benefits for awarded condition* | | ✓ |
| Integrated Personnel Support Centres | ✓ | ✓ |
| Transition interview | ✓ | |
| Operational Stress Injury Clinics | ✓ | ✓ |
| Operational Stress Injury Social Support | ✓ | ✓ |
| VAC Assistance Line | ✓ | ✓ |
| Disability Award | ✓ | ✓ |
| Veterans Independence Program | ✓ | ✓ |
| Career Transition Services | ✓ | ✓ |
| Public Service Health Care Plan | | ✓ |
| Long-Term Care | | ✓ |
| Rehabilitation Program (medical, psycho-social, and vocational) | | ✓ |
| Financial Benefits (for example, earnings loss, permanent impairment allowance, supplementary retirement benefit, CF income support) | | ✓ |

*An awarded condition is a service-related injury or illness for which Veterans Affairs Canada has granted a Disability Award.

Source: Department of National Defence and the Canadian Forces, and Veterans Affairs Canada

Universality of Service principle—Canadian Forces members must be able to perform general military duties and common defence and security duties, not just the duties of their military occupation or occupational specification. This may include, but is not limited to, the requirement to be physically fit, employable, and deployable for general operational duties.

4.6 An ill or injured Forces member who cannot perform tasks required by the **Universality of Service principle** and by the member's military occupation is assigned an employment limitation for a medical reason. If the limitation is judged to be permanent after the member's health condition has stabilized, an administrative review is launched to determine the most appropriate course of action:

- retention with or without restrictions,
- transfer to another military occupation, or
- release from the Forces.

4.7 According to National Defence and the Canadian Forces, during the six years from 2006 to 2011, a total of 98,866 Forces members were released, including 8,026 who were released for medical reasons. Other Forces members who were released for other than medical reasons may subsequently develop physical and mental health problems associated with their military service.

4.8 After leaving the Forces, members who are released for medical reasons are entitled to receive a long-term disability benefit for up to two years (or up to age 65 if totally disabled). They are also eligible to participate in the SISIP Vocational Rehabilitation Program for six months prior to release and for up to two years if they apply within 120 days after release. While in that program, they are also eligible to receive medical and psychosocial support under the Veterans Affairs rehabilitation program. Members released for medical reasons are automatically eligible for the Veterans Affairs rehabilitation program if they apply within 120 days after release. Beyond that period, applicants to the Veterans Affairs program must demonstrate that their rehabilitation needs are attributable to military service.

4.9 According to Veterans Affairs, its programs and services are based on modern rehabilitation principles. Any veteran with complex needs or anyone in the rehabilitation program is to be assigned a case manager and to undergo assessments as required. The case manager is to develop a realistic plan with the veteran and to monitor progress against agreed-upon objectives.

4.10 Veterans Affairs does not provide direct care, except at Ste. Anne's Hospital in Quebec. Veterans receive the health services to which they are entitled as provincial or territorial residents, and Veterans Affairs provides additional funding for services that the provinces or territories do not cover.

Operational stress injury—A broadly descriptive category rather than a diagnostic term. The term refers to any persistent psychological difficulty resulting from operational duties performed by a Forces member. It is used by National Defence and the Canadian Forces and by Veterans Affairs for a broad range of problems that result in impaired functioning. Included are diagnosed medical conditions such as depression, post-traumatic stress disorder, and anxiety or panic attacks, as well as less severe conditions.

4.11 In response to the increasing prevalence of operational stress injuries, National Defence has established seven Operational Trauma and Stress Support Centres across Canada, and Veterans Affairs has established 10 Operational Stress Injury Clinics. Forces members and veterans can be referred to either.

Estimated annual cost of support

4.12 The total annual cost of support for eligible ill and injured Forces members and veterans making the transition to civilian life is unknown because the expenditures are not tracked separately. Instead they are embedded within the overall costs of services, benefits, and administration provided by National Defence and the Canadian Forces, and by Veterans Affairs, in connection with supporting ill and injured Forces members and veterans in general. However, using unaudited departmental figures of amounts spent on key programs and benefits (disability awards, earnings loss benefits, the rehabilitation program, and Integrated Personnel Support Centres), we estimate that the costs were approximately \$500 million in the 2010–11 fiscal year.

Focus of the audit

4.13 Our audit objective was to determine whether National Defence and the Canadian Forces, and Veterans Affairs Canada adequately manage selected services and benefits to support eligible ill and injured Canadian Forces members and veterans in their transition to civilian life.

4.14 The audit focused on three areas:

- the ways in which the two organizations manage aspects of their service delivery. We paid particular attention to the case management services at Veterans Affairs because, according to the Department, this service is the foundation and key to the successful delivery of the New Veterans Charter;
- performance measurement and reporting; and
- the ways in which National Defence and the Canadian Forces, and Veterans Affairs coordinate transition support to ill and injured Forces members and veterans.

4.15 We did not look at whether Canadian Forces members and veterans received all the benefits and services for which they were eligible. We also did not examine the fairness of departmental services and benefits available to eligible Forces members and veterans, or the quality of medical treatment and care provided.

4.16 More details about the audit objective, scope, approach, and criteria are in **About the Audit** at the end of this chapter.

Observations and Recommendations

Service delivery

4.17 We examined whether National Defence and the Canadian Forces, together with Veterans Affairs Canada, have service commitments and delivery standards that are met and communicated to all Forces members and veterans, and whether the delivery approaches support an efficient transition and continuity of care, taking into account the assessed needs of ill and injured Forces members and veterans.

The transition process is complex

4.18 Staff at both departments told us that the transition process is complex. They must deal with a large number of departmental policies and procedures, which often change. As a result, employees find it increasingly difficult to understand the process and keep up to date. Some were concerned they might make decisions or provide advice on the basis of outdated information or without having considered all relevant policies.

4.19 In interviews, veterans voiced concerns about

- the complex eligibility criteria,
- the lack of clear program and benefits information,
- the amount of paperwork needed to access programs and benefits, and
- the length of time it takes to access programs and receive benefits.

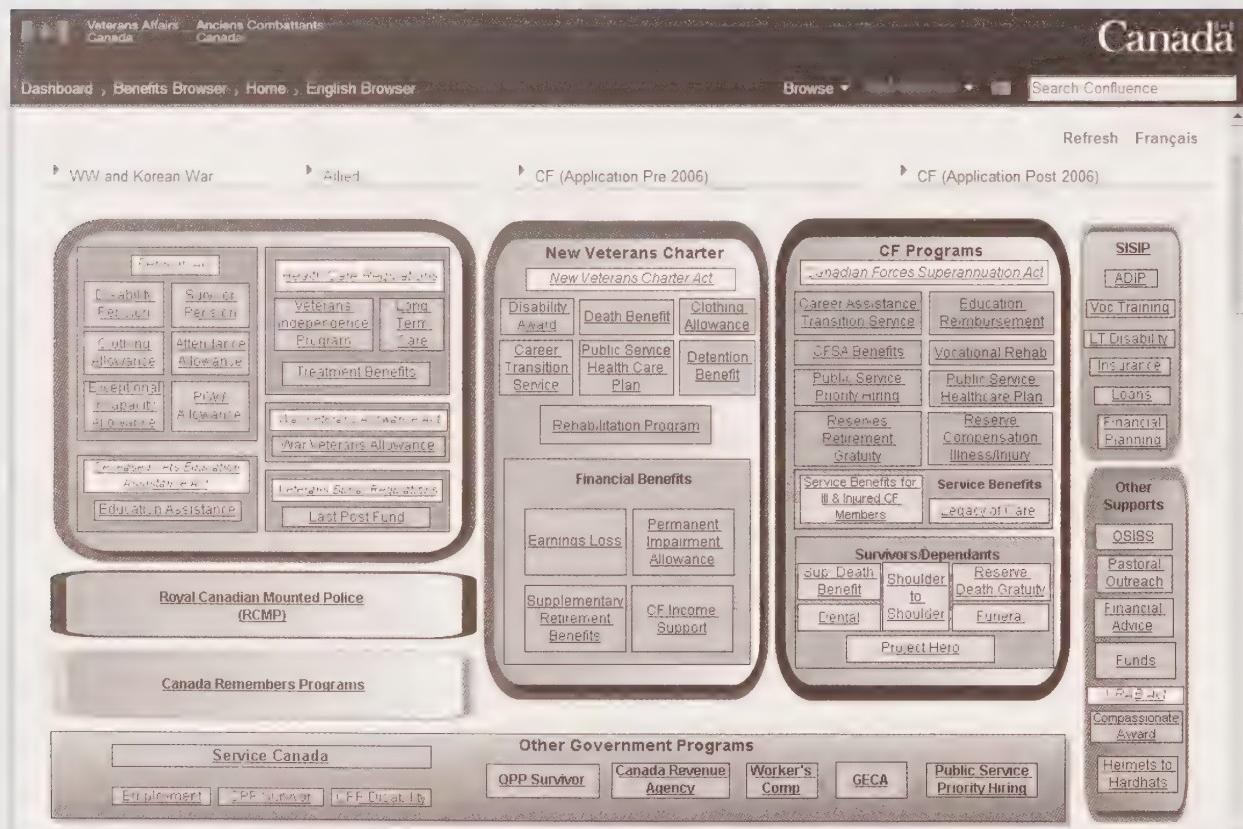
4.20 The current application process at Veterans Affairs Canada creates an administrative burden for Forces members and veterans. They have to submit applications and supporting documents for each of their medical conditions to access different programs and benefits. This approach can be time-consuming and may delay access to programs and benefits.

4.21 Several veterans also mentioned that they needed help to fill out various forms. They often had to telephone Veterans Affairs for clarification and guidance. We assessed the complexity of the language used to describe some departmental services and benefits for applicants, including documents from both National Defence and Veterans Affairs websites. We reviewed their content, using a language complexity

analysis tool. The findings indicated that some documents used language best suited to individuals with some post-secondary education. However, only 15 out of 80 (about 20 percent) of the Forces members and veterans whose files we reviewed had education beyond the high-school level.

4.22 One tool that could help Veterans Affairs provide more accurate and timely service is the Benefits Browser, a software application being reviewed by the Department but not yet implemented (Exhibit 4.2). During our field visits, a client service agent using a test version told us that with this tool he could find up-to-date information much more quickly and had to refer far fewer calls to other staff members. The Browser greatly cuts the volume of documentation needed by agents.

Exhibit 4.2 The Benefits Browser (software application)



Source: Veterans Affairs Canada

4.23 Recommendation. National Defence and the Canadian Forces, and Veterans Affairs Canada should streamline and automate their transition policies and administrative processes to make it easier for ill and injured Forces members and veterans to access programs and benefits in a timely manner.

National Defence and Canadian Forces' response. Agreed. The recently published document, *Caring For Our Own: A comprehensive approach for the care of CF ill and injured members and their families*, and the regularly updated booklet, *Death and Disability Benefits, Programs and Services: A Guide for Serving and Former Canadian Forces Personnel and Their Families*, are illustrative of our efforts in consolidating policy and procedural information and communicating it in non-technical terms. In collaboration with Veterans Affairs Canada, National Defence and the Canadian Forces will continue to streamline and, where practical, automate transition policies and administrative processes.

Veterans Affairs Canada's response. Agreed. Veterans have told us they want a more hassle-free system, and the Department is committed to delivering this. Through the Transformation Agenda, all programs, policies, and business processes are under review. Measures to cut red tape, overhaul service delivery, and improve technology platforms mean that veterans and their families will get faster, one-stop access to information and support when they need it and for as long as they need it. For example:

- Veterans now can visit any of Service Canada's 600 points of service for information on programs or help applying for benefits.
- Some 80 percent of calls to the Department are answered within two minutes.
- Benefits are being delivered faster. Most disability applications are processed within 16 weeks, 30 percent faster than before. Most rehabilitation applications are processed in two weeks or less, 50 percent faster than before.
- More avenues have been identified to support homeless veterans.

By March 2013, the Department will do the following:

- review, revise, and reduce the number of policies guiding the delivery of benefits. Policies will offer clear, modern-day solutions to veterans' needs, and will foster greater harmony related to the spectrum of health care benefits available to serving and released Canadian Forces members;

- better streamline and coordinate services through each of the 24 Integrated Personnel Support Centres so that injured and ill Canadian Forces members and veterans have faster, more seamless access to the benefits they need;
- make it easier for individuals to be referred to the network of mental health clinics operated by Veterans Affairs Canada and National Defence; and
- further improve turnaround times to 12 weeks for disability benefit decisions.

4.24 Recommendation. National Defence and the Canadian Forces, and Veterans Affairs Canada should continue to simplify the language that explains the support available to ill and injured Forces members and veterans. They should ensure that information is updated and communicated to staff and potential beneficiaries, as appropriate, using online tools such as the Benefits Browser.

National Defence and Canadian Forces' response. Agreed. National Defence and the Canadian Forces are taking action to address this recommendation. A new, user-friendly website designed to communicate information on benefits and programs in clear and concise language is under development. We will undertake a review during 2013 of pamphlets, information booklets, and other hard-copy materials made available to Canadian Forces members and their families to ensure that information on benefits and programs is up to date and understandable. Additionally, the outreach briefings provided to Regular and Reserve Force units will be reviewed for currency and clarity. The feasibility and resource implications of including formal readability reviews as part of the development process for any new information tools will also be investigated during 2013.

Veterans Affairs Canada's response. Agreed. Veterans Affairs Canada believes veterans have the right to access information that is clear and easy to understand. As part of the Department's ongoing commitment to reach out to veterans and their families:

- Work has accelerated to simplify disability benefit decision letters, as well as decision letters related to health care and home care benefits. This builds on work that began in 2009.
- By March 2013, veterans and their families will find it easier to apply online for benefits and navigate the website with the help of a new Benefits Browser that simplifies the process of gathering information about programs and policies.

- A similar type of Benefits Browser already is being used internally by staff to help them access relevant information online to serve veterans more quickly.
- Work is well under way to simplify forms and minimize the amount of paperwork that veterans and families must submit.
- In cooperation with National Defence, the Canadian Forces, and other service partners, the Department also will continue to attend events and information sessions across the country to share clear information on benefits and services with veterans, still-serving personnel, and their families.

Problems exist with information sharing and data reliability

4.25 National Defence and the Canadian Forces, and Veterans Affairs Canada recognize the importance of having reliable and timely information. They acknowledge the need to improve their information-sharing systems and have identified an initiative, the Transfer of Electronic Health and Administrative Records, as a joint priority. Under this priority, they aim to streamline interdepartmental functions and have recently started a pilot project to transmit medical data electronically. In the next few years, this streamlining may take the form of improved business processes, new tools, and/or electronic data exchange. Meanwhile, more needs to be done to ensure that information on Canadian Forces members is accurate and that authorized information is passed to Veterans Affairs in a timely manner.

4.26 The Canadian Forces service number is the main identifier used by National Defence and the Canadian Forces to create and retrieve records on military personnel. Veterans Affairs uses some information contained in a Forces member's records for tasks such as determining eligibility and support level. While we were selecting a sample of cases for review from the Veterans Affairs rehabilitation database, we noted that approximately 1,650 (24 percent) of the service numbers were inaccurate or missing. We also found errors in key data originating with National Defence and the Canadian Forces, and used by Veterans Affairs to determine eligibility for its rehabilitation program—for example, type of Forces service (regular or reserve), date of release, and release item. Of the 50 rehabilitation cases that we reviewed, we found that the two departmental databases contained inconsistent data about the same Forces member in 9 cases (18 percent). The data concerned release dates, release items, or service in special duty areas—matters that could affect services and benefits.

Special duty area—An area outside of Canada where Canadian Forces members are exposed to conditions of elevated risk not normally associated with service in peacetime.

4.27 We also noted that National Defence and the Canadian Forces provided information to Veterans Affairs mainly in paper rather than electronic format. Medical files may be stored at locations across the country. When a medical file is requested, it must be located, photocopied, and reviewed to remove third-party personal information. This paper-based approach delays information transfers and increases the risk of error.

4.28 Recommendation. National Defence and the Canadian Forces, and Veterans Affairs Canada should ensure that their databases contain reliable data about Forces members, and that Canadian Forces and Veterans Affairs processes are managed to facilitate the timely and efficient sharing of authorized information.

National Defence and Canadian Forces' response. Agreed. In close cooperation with Veterans Affairs Canada, National Defence and the Canadian Forces will continue to improve business processes and implement new tools to facilitate the maintenance of accurate information and the timely and efficient sharing of such information. The primary Canadian Forces database for casualty administration is the Mission Support System. It is currently being upgraded and is expected to be rolled out in early 2013. In the area of medical information, Veterans Affairs Canada and the Canadian Forces currently have a joint project under way that will enable the disclosure of Canadian Forces members' personal health information to Veterans Affairs Canada in a more efficient, centralized, and trackable way. The intent is to conduct pilot tests in fall 2012, and undertake nationwide implementation in 2013. Methods for ensuring database accuracy will be reviewed as integral elements of these programs.

Veterans Affairs Canada's response. Agreed. Sharing information internally and with the Canadian Forces through a secure electronic environment is a key initiative under the Department's Transformation Agenda.

- In 2012, the Canadian Forces service number that individuals receive when they join the military has become the standard way to identify those who later apply for departmental benefits. This will make it easier to track the benefits and services veterans receive over their lifetime, leading to better continuity of care, accurate information sharing, and better privacy safeguards.
- The switch to electronic records already is under way. To date, more than two million pages of veterans' files have been scanned.

- In July 2012, the electronic transfer of still-serving members' files began at two Canadian Forces bases. Already, the positive results from these pilots suggest that the national rollout to another 21 bases may conclude well ahead of the scheduled completion date of 2015.
- By 2015, or before, the time to transfer records will drop from seven weeks to one week, further accelerating the decision-making process so that veterans receive faster access to benefits.

Policies and processes at the Integrated Personnel Support Centres have not been fully implemented

4.29 Since March 2009, National Defence and the Canadian Forces, under the direction of the VAC-DND Steering Committee (see paragraph 4.68), have established 24 Integrated Personnel Support Centres and 9 satellites across the country. The centres are intended to provide ill and injured personnel with dedicated supervision and access to a set of support services—for instance, support for returning to work, outreach, casualty support, and advocacy services. The centres have a one-stop approach and incorporate Veterans Affairs staff. The aim is to ensure comprehensive and consistent support.

4.30 In interviews, veterans and staff at both departments spoke positively about the role of the support centres. With Veterans Affairs staff available on the base, Forces members have the opportunity to learn more about the transition support available to them and all parties can come together in one place to coordinate support.

4.31 We visited three centres. We observed that service delivery varied from one centre to another. Delivery depended heavily on personal relationships between staff of Veterans Affairs and the Canadian Forces, as well as between staff at the centres and the base. For example, we observed different casualty tracking practices at different centres. In some centres, staff members actively sought information. In other centres, they were uncertain of their authority to do so and therefore took a less active approach. In our view, until the departments fully implement formal policies and processes for coordinating service delivery, it will be difficult to ensure that Forces members and veterans receive comprehensive and consistent support across Canada.

4.32 Staff responsibilities at the centres continue to evolve. We found that in some cases, these responsibilities have not been fully implemented. For example, employees have recently been given the responsibility of developing integrated transition plans for members who are severely ill or injured, with complex needs. However, in the

three centres we visited, we found that staff had not yet developed any integrated transition plans and they had not been given guidance on how to create these plans.

4.33 Recommendation. National Defence and the Canadian Forces, and Veterans Affairs Canada should develop and implement policies and processes for coordinating the delivery of services to Forces members and veterans at the Integrated Personnel Support Centres.

National Defence and Canadian Forces' response. Agreed. The requirement to develop integrated transition plans was announced on 11 October 2011. Guidance was issued, via a Canadian Forces directive, on 30 October 2011, to assist all Integrated Personnel Support Centres in developing integrated transition plans for their clients. Business processes and standard operating procedures in this area have been, and will continue to be, reviewed, standardized, and implemented as the Joint Personnel Support Unit framework evolves, with a target date of December 2013 for completion of this effort.

Veterans Affairs Canada's response. Agreed. Already, staff from Veterans Affairs Canada, National Defence, and the Canadian Forces work side by side to support up to 1,300 injured and other Forces members and veterans who contact the national network of 24 Integrated Personnel Support Centres each month.

Operational guidelines for the centres are already in place. As of October 2011, integrated transition plans are offered to all severely injured and ill personnel, although not all accept the offer. The role of the Veterans Affairs case manager is well established in this process.

Since the first centres were launched in 2009, all partners have learned a great deal about how best to support those who are injured and ill. In 2013, the best practices that have been developed will be used to fully implement a set of common business processes and practices across the network of centres. This will further streamline and coordinate the delivery of programs and services to all those who seek support.

The Canadian Forces is not fully meeting its case management requirements and service standards

4.34 According to National Defence and the Canadian Forces, the goal of case management is to ensure that all eligible Forces members have access to and knowledge of the scope of services and benefits available to them. Case managers

- assess the members' health needs and reassess them when required;

- develop and monitor a case plan;
- inform members about available programs and benefits; and
- in some cases, help members apply for related benefits.

4.35 We examined 80 case files to see whether Forces members received case management and related services for which they were eligible. We found a number of instances in which they did not (Exhibit 4.3).

Exhibit 4.3 Canadian Forces members did not always receive case management and related services for which they were eligible

| Canadian Forces service requirement | Non-compliance rate | Potential impact |
|---|---|--|
| Case management services: Any Forces member being released for medical reasons should receive case management services. | Of the sample of 80 cases, 54 Forces members were released for medical reasons. Of the 54 members, 7 (13%) did not receive case management services. | Without case management, a Forces member does not have access to certain services. |
| Case plan: Anyone who is receiving case management services should have a case plan. | Of the sample of 80 cases, 54 Forces members were released for medical reasons and 47 of these received case management services. Of the 47 members, 5 (11%) did not have a case plan. | If a Forces member does not have a case plan, steps might be missed in the release process—for example, applying to the Service Income Security Insurance Plan or the Veterans Affairs rehabilitation program within 120 days. |
| Reassessment: Anyone who is receiving case management services should be reassessed by a case manager. | Of the sample of 80 cases, 54 Forces members were released for medical reasons and 47 of these received case management services. Of the 47 members, 4 (9%) were not reassessed after an initial meeting. | If the Forces member does not receive regular follow-up, the case manager may not be aware of the client's current situation and potential need for support. |

4.36 We also looked at the 80 case files to determine whether the Canadian Forces met case management service standards. We found that service standards for assessments were not being met for most cases (Exhibit 4.4).

Exhibit 4.4 Canadian Forces case management service standards for assessments are not being met for most cases

| Canadian Forces service standard | Non-compliance rate | Potential impact |
|--|---|--|
| Initial assessment: The case manager should assess a Forces member within one week of referral. | Of the sample of 80 cases, 54 Forces members were released for medical reasons and 47 received case management services. Of the 47, 44 had a referral date for case management and 37 out of 44 referral dates (84%) did not meet the standard. | Delay in obtaining case management services. |
| Reassessment: The case manager must reassess the Forces member according to level of case complexity, with complex cases being reassessed more frequently. | Of the sample of 80 cases, 54 Forces members were released for medical reasons and 47 received case management services. Reassessments for 31 of the 47 cases (66%) did not meet the standard. | Services could be interrupted. According to Canadian Forces policy, members in the case management program should be monitored regularly to ensure continuity of services. |

The Canadian Forces has not set performance standards for decisions on employment limitations for medical reasons and on medical release

4.37 A key part of the process of release for medical reasons is the decision about employment limitations due to the member's medical condition. We found that there is no time limit for making the decision. Our file review showed that the time taken for this decision ranged from 14 days to 10 months, with an average of about 5 months. The next key decision in the process is the administrative decision on whether to release the member for medical reasons. We found that the time taken for the decision ranged from 12 days to more than six years, with an average of about 9 months. Departmental officials told us that because of the length of time it takes for an administrative decision to be made on medical release, some members choose to leave the Forces voluntarily. They thereby lose access to the additional support available to members who are released for medical reasons.

4.38 The lack of formal performance standards means that the Forces members do not know how long they have to wait for a decision. The lack of standards also makes it difficult to monitor and evaluate departmental performance. Questions could be raised as well

about perceived fairness and consistency, given the length of time it takes to reach decisions for different Forces members.

4.39 Under the new Career Transition Support Policy issued in October 2011, some severely ill or injured Forces members may continue to receive transition support from the Forces for up to three years after the final decision is made to release them. These are members who have permanent employment limitations for medical reasons and cannot meet the Universality of Service principle, and who also have complex transition needs. However, it is not clear how this extended retention period will contribute to a successful transition to civilian life—particularly since release is inevitable and the Veterans Affairs’ rehabilitation program stresses early intervention. In our file review, we found that Forces members were retained in the Forces for an average of about 10 months following the decision to release for medical reasons. The retention period ranged from 43 days to about three years.

4.40 Recommendation. National Defence and the Canadian Forces should develop and communicate service standards for the decision on employment limitations for medical reasons and the decision on medical release.

National Defence and Canadian Forces’ response. Agreed. Since May 2012, the Director of Military Careers Administration has been engaged in a complete review of the efficiency, effectiveness, and service delivery of administrative procedures. This will enhance the ability of the Canadian Forces to complete administrative reviews and to render decisions within improved timelines. While taking into consideration the average volume of files to be considered, essential procedural requirements, and staff resources available, National Defence and the Canadian Forces undertake to review, by March 2013, the feasibility of establishing service standards for typical non-complex cases, for both the medical employment limitation decision process and the medical release review process.

4.41 Recommendation. In consultation with Veterans Affairs Canada, National Defence and the Canadian Forces should evaluate how the new Career Transition Support Policy affects ill and injured members’ reintegration into civilian life.

National Defence and Canadian Forces’ response. Agreed. The provision of a seamless transition between partnering organizations, through improved communication and co-location, is one of the objectives identified in the Joint Personnel Support Unit performance

measurement framework. This framework will be further developed to ensure that we are able to assess whether the new transition policy is in fact meeting the requirements of our ill and injured personnel. Once the Mission Support System rollout is completed (current estimate is early 2013), the Canadian Forces and National Defence will be able to develop indicators of transition readiness, and in collaboration with Veterans Affairs Canada, will attempt to capture post-release information on how the Career Transition Support Policy affects reintegration into civilian life.

Veterans Affairs Canada's response. Agreed. Up to six months before release, Veterans Affairs case managers, in collaboration with National Defence and the Canadian Forces, help Forces members who are being released to access services. This early intervention gives members and their families the ability to transition from the military to civilian life as seamlessly as possible. Once they are released, veterans may qualify for Veterans Affairs Canada's Rehabilitation Program, where the focus is on assessing their needs, rehabilitating them to the fullest extent possible, and then linking them with vocational rehabilitation experts who can help them prepare for a meaningful civilian career.

Veterans Affairs Canada also is working with the business community and various not-for-profit organizations to create more employment opportunities for Forces members who are being released and former Forces members.

Veterans Affairs Canada will continue to assist and support National Defence and the Canadian Forces, as appropriate, in their efforts to further assess if the Career Transition Support Policy is, in fact, meeting the requirements of ill and injured personnel.

Veterans Affairs case management services need improvement

4.42 Veterans Affairs Canada is responsible for implementing the New Veterans Charter, which came into effect on 1 April 2006. The Charter provides a medical, psychosocial, and vocational rehabilitation program, supported by case management services. It also provides financial benefits to offset the loss of earnings, as well as disability awards, survivor benefits, and group health insurance. In 2005, Veterans Affairs reported that it had developed sufficient business processes and was implementing a comprehensive training plan to prepare for implementation of the Charter. We reviewed how Veterans Affairs was handling case management. We found opportunities to improve key elements of this important service.

4.43 According to Veterans Affairs policy, within six months before release the Department should offer a transition interview to all Regular Force members who are being released for any reason and to Reserve Force members who are being released for medical reasons. It is the responsibility of the Forces member to attend the interview. The purpose of the interview is to

- identify potential barriers to a successful return to civilian life,
- inform the Forces member of the range of services and benefits available, and
- identify anyone at risk who may require Veterans Affairs case management services.

4.44 In our sample of 80 cases, 70 members should have been offered a transition interview. We identified 6 (9 percent) who did not receive this interview.

4.45 According to Veterans Affairs, veterans enrolled in the rehabilitation program are required to be assessed and provided case management services. In our review of files, we found that of the 50 veterans enrolled in the rehabilitation program, 49 had needs assessments completed and 1 veteran had not. Consultations between the case manager and other experts, such as medical officers and mental health specialists, are required when a veteran has health needs that are not being met or there is a change in medical condition. Of the 49 veterans with completed assessments, we found that, according to the Department's documents, 38 had at least one unmet need identified. But, there was no documentation of any consultation for 15 of the 38 veterans (40 percent).

4.46 During our field visits, Veterans Affairs medical officers expressed concern that needs assessments were being performed by staff without the advice of qualified experts when required, especially for veterans with mental health issues. The officers were also concerned that they were not being consulted at appropriate times—for example, during the development of the case plan. We noted that while it is required to document interdisciplinary assessments, there is no requirement to document the advice received or the action taken in response to that advice. This raises the risk of inappropriate referrals and inefficient use of available resources.

4.47 We visited two operational stress injury clinics. At one of them, we were told that 3 of 21 case managers made the majority of referrals to the clinic and that the facility could serve approximately 50 percent more clients at no extra cost to Veterans Affairs. At the second clinic,

we were told that some case managers actively made referrals, while others refrained from referring clients who could benefit from the clinic's services.

4.48 The case plan helps the veteran and the case manager focus on achieving agreed-upon, documented goals. According to Veterans Affairs, a case plan is to be prepared for any veteran identified as being at risk of not successfully returning to civilian life or any veteran enrolled in the rehabilitation program. Of the 68 Forces members who had transition interviews (from our sample of 80 cases), 20 were identified as being at risk of unsuccessful re-establishment. We found, however, that no case plans had been prepared for 4 of the 20 (20 percent). In addition to these 4, there were 4 veterans in the rehabilitation program for whom no case plans had been prepared. Therefore, the required case plans were lacking for a total of 8 out of 54 (15 percent), and there was no explanation on file as to why. Without a case plan, it is difficult for the case manager to track progress and ensure that the veteran's needs are being met.

4.49 Veterans Affairs specifies 10 components of case planning and monitoring to be carried out by the case manager with the veteran (Exhibit 4.5). For the 45 case plans developed, we reviewed whether managers had carried out the required components. We found that not all of the components had been fully implemented in the case plans we reviewed. Components with high completion rates included an overview of the situation, identifying desired outcomes, and progress notes. Components with low completion rates included evidence of signed consent and action steps taken. These low completion rates may indicate a need to improve documentation or a lack of emphasis on achieving rehabilitation goals.

4.50 In interviews, Veterans Affairs service delivery staff told us of their concern about the lack of a formalized departmental process for identifying and dealing with the many changing policies, procedures, and guidelines pertinent to their work. Some felt that there was no cohesive understanding at Veterans Affairs of what case management means, and that the roles and responsibilities of case managers and other staff were not clearly defined. In January 2012, Veterans Affairs set out the roles and responsibilities for service delivery staff, including case managers and client service agents. Veterans Affairs reported that it was developing the roles and responsibilities of other service delivery staff at the district, regional, and national levels, including health professionals.

4.51 In 2010, the Veterans Affairs National Case Management Unit reviewed case management practices in four regions. The resulting report referred to gaps that made it difficult for case management services to fully support clients' rehabilitation progress. The gaps included

- the absence of case planning for mental health issues,
- the lack of clarity concerning family and community roles in case planning, and
- the lack of understanding of how pain influences the ability to function.

Exhibit 4.5 Completion rates for some key components of Veterans Affairs case plans were low

| Veterans Affairs key case plan components | | Description | Percentage of cases where the component was complete in the case plan (out of 45 case plans) |
|--|---|---|--|
| 1 | Overview of the situation | Veteran's self-identified needs and concerns, genetics and environmental risks, challenges and strengths, family and social support, etc. | 98% |
| 2 | Client's goals: Where do you want to be? (what and how) | Realistic and specific long-term goals are set. | 78% |
| 3 | Barriers: What is preventing you from getting there? | Identify the elements and obstacles that are preventing the veteran from meeting the long-term goals. | 76% |
| 4 | Desired outcomes | Outcomes are set and oriented toward a goal the veteran wishes to achieve. | 93% |
| | | The outcomes are specific, measurable, attainable, realistic, and timely (SMART). | 26% |
| 5 | Action steps: due date, completed or in progress | Break down desired outcomes into manageable activities, and follow up according to due dates or at least every 90 days. | 49% |
| 6 | Veterans Affairs agreement with the veteran | A signed commitment between the case manager and the veteran to abide by the case plan. | 22% |
| 7 | Resources | Document services and benefits being provided to the veteran. | 89% |
| 8 | Indicators of success | Significant milestones the veteran has achieved toward completing the desired outcomes. | 31% |
| 9 | Progress notes, consultations, etc. | Direct contact should occur with the veteran at least every 90 days. | 80% |
| 10 | Disengagement | Document the plan for disengagement. | 20% |

4.52 The report also noted weaknesses in case planning, service coordination, and monitoring and evaluation. Veterans Affairs has undertaken several initiatives to address gaps and weaknesses in case planning. These include developing case planning guidelines as well as a case management performance measurement plan and framework. However, there is no department-wide quality management system in place.

4.53 Recommendation. Veterans Affairs Canada should clarify and communicate the roles and responsibilities of all parties involved in the case management service. It should develop and implement a department-wide quality management system for this service.

Veterans Affairs Canada's response. Agreed. The ability to monitor and measure the success of the case management function is a priority for the Department and a cornerstone of the Transformation Agenda. To strengthen support to veterans with more complex needs:

- Roles and responsibilities have been clarified for Veterans Affairs' client service team members. As business processes and veterans' needs evolve, roles and responsibilities will continue to be adjusted and communicated to all those involved in the case management process.
- Veterans enrolled in the Rehabilitation Program have faster access to benefits that are part of their case plan now that case managers have been empowered to make more decisions without additional approvals.
- Processes and standards are in place to give all case-managed veterans more access to their case manager.
- National training and learning tools are in place, and more are planned for 2012–13.
- National monitoring processes will be reviewed and adjusted, as needed, to continue to ensure that case management is delivered as intended.

Performance measurement and reporting

4.54 We examined how well National Defence and the Canadian Forces, and Veterans Affairs Canada measure and report on performance, and use the performance information to improve the management of programs and services offered to ill and injured Forces members and veterans in their transition to civilian life.

The Canadian Forces does not maintain consolidated information on ill and injured members, and some administrative data is unreliable

4.55 The Canadian Forces does not maintain consolidated information on all ill and injured Forces members, including members with permanent medical employment limitations, those receiving case management services, those who will be released for medical reasons, and those receiving transition support services. Some of this information is currently contained in individual medical files, while administrative information is contained in several databases. Consequently, the Canadian Forces does not have readily available information to efficiently manage programs and services and to support ill and injured Forces members in their transition.

4.56 In addition, according to Canadian Forces Health Services staff, the poor quality of some Canadian Forces data limits the ability to forecast the demand for services and measure effectiveness. For example, data on reservists was so poor that they had to be excluded from the May 2011 report, *Canadian Forces Cancer and Mortality Study: Causes of Death*. We were also told that the administrative data on deployments was not sufficiently reliable for use in studies such as the November 2011 report, *Cumulative Incidence of Post-Traumatic Stress Disorder (PTSD) and Other Mental Disorders in Canadian Forces Personnel Deployed in Support of the Mission in Afghanistan, 2001-2008*. We noted that the lack of reliable data was acknowledged in June 2009, when the *Report on the Evaluation of Support to Injured CF Members and their Families* stated, “The extent to which statistics are kept is uneven at best.”

4.57 Recommendation. National Defence and the Canadian Forces should maintain consolidated information on ill and injured Forces members who will be released for medical reasons to help better manage programs and services to support their transition.

National Defence and Canadian Forces' response. Agreed. The Canadian Forces remain committed to ensuring our programs and services are meeting the needs of our ill and injured Forces members. The Joint Personnel Support Unit's performance measurement framework will continue to be used as the blueprint for the measurement, evaluation, and reporting of program and service performance. Surveys administered to Joint Personnel Support Unit clients and the local chain of command will be used to assess the utility of programs and services from a user perspective. There are also a number of projects under way that are designed to improve the consolidation of personal health information, in accordance with the

Privacy Act, as well as a project to ensure that all Reserve documents are available electronically in the Canadian Forces Health Information System by the end of 2012. A new policy mandating that all new forms go through a standardized approval process to prevent the proliferation of separate systems and non-standardized forms is expected by fall 2012. Finally, a quality assurance program is now being developed for rollout at the local level, with headquarters oversight and guidance, in 2013.

The Canadian Forces has not yet fully addressed important issues to improve management of its support for the transition to civilian life

4.58 Information is available to monitor some aspects of the performance of Canadian Forces programs and services supporting the transition of ill and injured Forces members. However, we found that issues previously identified have not yet been fully addressed. The June 2009 evaluation report identified issues concerning difficulties in monitoring individuals during and after release, and noted that some vulnerable Forces members had been without Canadian Forces or Veterans Affairs Canada support during their transition to civilian life. The Canadian Forces developed action plans in response to the recommendations in the report. However, our work, including interviews with veterans, confirmed that these issues persist, particularly in the case of reservists.

4.59 Recommendation. National Defence and the Canadian Forces, in cooperation with Veterans Affairs Canada, should continue to improve management of its support for the transition to Veterans Affairs Canada of ill and injured Forces members, particularly reservists.

National Defence and Canadian Forces' response. Agreed. While recognizing that Canadian Forces responsibility for follow-up formally ends when a member is released, ill and injured members will be tracked by the Canadian Forces until an individual returns to unrestricted duty; a former Canadian Forces member (including reservists) is able to resume or seek employment; a member is able to cope independently without any further assistance; or a member expresses that he or she no longer wishes any further contact. By June 2013, the Canadian Forces and National Defence will review procedures to ensure that, when required or appropriate, members who are being released for medical reasons, especially reservists, successfully make the transition to Veterans Affairs Canada care. In partnership with Veterans Affairs Canada, the Canadian Forces and National Defence will, also by June 2013, examine options to improve systematic post-release follow-up.

Veterans Affairs Canada's response. Agreed. In collaboration with National Defence and the Canadian Forces, work is ongoing to

- provide ill or injured members with immediate and ongoing support through all stages of recovery, rehabilitation, and reintegration into civilian life;
- offer transition interviews to Regular and Reserve Force members who are being released, and their families, and encourage them to attend; and
- provide members who are being released for medical reasons or those who have not been able to make a successful transition with timely access to Veterans Affairs Canada's Rehabilitation Program.

In 2013, the Department

- will collaborate with National Defence and the Canadian Forces to examine options to further improve systematic post-release follow-up; and
- in collaboration with National Defence and the Canadian Forces, will partner with Statistics Canada to conduct research on the transition experience of former reservists. This is a follow-up to the 2011 Life After Service Study, which included an increased focus on reservists in addition to Regular Force veterans. Going forward, these research findings will add to the Department's understanding of how to design, implement, and deliver policies, programs, and business processes that best meet the needs of ill and injured personnel, including reservists.

Performance reporting on Veterans Affairs service delivery is incomplete

4.60 The Veterans Affairs Canada website provides information on service standards for processing times for applications to selected programs, including targets. However, the Department has not reported on its performance against those targets on its website since the 2007–08 fiscal year. As a result, veterans lack information about the length of time actually required to process applications. For example, our sample of 80 cases included 50 participants in the Veterans Affairs rehabilitation program. We found that in 34 of the 50 cases (68 percent) we reviewed, the Department did not meet applicable service standards for making a decision on the complete rehabilitation application.

4.61 Further, in its 2010–11 Departmental Performance Report, Veterans Affairs stated that it was able to reduce the average time required for decisions on disability applications from 24 weeks to 16 weeks, but it did not explain how it achieved the reduction. In the 2010–11 fiscal year, the service standard was 24 weeks measured from the date the Department received the application. As of 1 April 2011, we noted that the service standard was reduced to 16 weeks but the period is now measured from the date on which Veterans Affairs considers it has received all the information required to support the application. We reviewed 22 applications for disability awards submitted in 2010–11 and found that the average processing time measured from the date of the application to the time of the decision was 21 weeks. The Department in fact reduced the average time for decision making on disability applications for our sample of cases. However, from the perspective of veterans, it is not clear whether service delivery actually improved as much as reported by the Department or whether some of the decrease was due to the change in the way the processing time was calculated.

4.62 Recommendation. Veterans Affairs Canada should publicly communicate performance against service standards.

Veterans Affairs Canada's response. Agreed. By May 2013, the Department will formally post its performance against all published service standards for the 2012–13 fiscal year on the Department's website. These results will be updated every year.

Veterans Affairs' forecasting of clients and expenditures for New Veterans Charter programs needs improvement

4.63 Veterans Affairs Canada produces an annual Client and Expenditure Forecast, which it uses to support planning. The Department has identified a high variation in the accuracy of forecasts for New Veterans Charter programs (Rehabilitation and Financial Benefits) for the last three years. According to the Department, it does not have enough performance information to consistently assess trends and provide forecasts. The forecasts relied on historical data; however, other factors also contribute to the variation in the accuracy of the forecasts.

4.64 We noted that past Veterans Affairs forecasts did not take into account information about the increasing number of Canadian Forces members with mental health issues, such as post-traumatic stress disorder. In our view, this would help to improve the accuracy of the forecasts. It also underscores the need for the Department to cooperate

more closely with the Canadian Forces. In developing forecasts, it is important for Veterans Affairs to make better use of information about the expected number of ill and injured Forces members who will need its support.

4.65 We also noted that veterans are staying in the rehabilitation program longer than the two years estimated by Veterans Affairs at the time of approval of the New Veterans Charter. The Department recognizes the situation but it has not fully determined the impacts on veterans' reintegration into civilian life and on future program funding requirements for the New Veterans Charter.

4.66 Recommendation. Veterans Affairs Canada should improve its client and expenditure forecasting for the New Veterans Charter programs.

Veterans Affairs Canada's response. Agreed. As part of the action plan to improve the accuracy of client and expenditure forecasting, the Department will continue to

- expand partnerships and consultation with National Defence and the Canadian Forces to source all possible data relevant to forecasting methodologies;
- validate forecasting assumptions and methodologies through an independent third party; and
- continue to partner with National Defence, the Canadian Forces, and Statistics Canada on a series of research projects to better understand the transition experience of both Regular and Reserve Force members. This follow-up to the 2011 Life After Service Study will include data on the overall veteran population, not just those who receive departmental benefits, allowing for a broader understanding of veterans' health and wellness over their lifetime. In addition, the current study will place increased emphasis on reservists, a group making up about 50 percent of Canada's overall population of veterans.

Governance and coordination

4.67 We looked at whether National Defence and the Canadian Forces, and Veterans Affairs Canada have an overarching governance framework to coordinate, harmonize, and communicate the various services and benefits available to ill and injured Forces members and veterans.

4.68 In 1999, the Chief of Military Personnel and his counterparts at Veterans Affairs put in place a steering committee, the VAC-DND Steering Committee, to help manage the evolving needs of Forces

members and veterans. The stated purpose and objective of the committee is to identify and manage joint priorities and to be a decision-making body that will enable seamless transition and reintegration, and will provide continuity of support during the release from the military to civilian life. The co-chairs of the committee are Veterans Affairs' Assistant Deputy Minister of Service Delivery and the Canadian Forces Chief of Military Personnel.

Gaps exist in the overarching governance framework

4.69 There are three gaps in the overarching governance framework. They concern the committee's mandate, the management of joint priorities, and information sharing.

4.70 Committee's mandate. The committee's terms of reference do not specify the scope of its delegated decision-making authority and what it is accountable for. Consequently, accountability for the committee's decisions and how it manages joint priorities is unclear.

4.71 Joint priorities. We found that there are long-standing joint priorities for which the committee has no clear measurable objectives, and it has only recently set timelines for completion for some priorities. Examples include

- harmonizing policies and programs,
- developing joint mental health and outreach strategies, and
- transferring electronic health and administrative records.

Although progress has been made, we noted that none of these priorities has been completed.

4.72 Information sharing. There is no formal requirement in the committee's terms of reference to consult and share information on proposed policy and program changes in each department that could affect the transition of ill and injured Forces members and veterans, or the benefits and services they receive. This situation increases the risk of overlaps and gaps in continuity of care. It could also have unintended effects that impede successful transitions.

4.73 Recommendation. National Defence and the Canadian Forces, and Veterans Affairs Canada should update the joint steering committee's terms of reference to specify its authority, responsibility, and accountability.

National Defence and Canadian Forces', and Veterans Affairs Canada's response. Agreed. By March 2013, National Defence and the Canadian Forces, and Veterans Affairs Canada will update the terms of reference for the committee to ensure a clear delineation of committee authority, responsibility, and accountability.

4.74 Recommendation. For each approved joint priority, the steering committee should establish measurable objectives and specific timelines for completion. It should prepare an annual report to the Deputy Ministers and the Chief of the Defence Staff, summarizing progress achieved against the joint priorities.

National Defence and Canadian Forces', and Veterans Affairs Canada's response. Agreed. In 2011, the joint steering committee identified objectives and timelines for seven priorities: continuity of care; transition management; transfer of electronic Canadian Forces personnel records; a joint mental health strategy; outreach, consultation and engagement; commemoration; and research. These priorities continue to evolve as progress is achieved and new plans are developed.

In 2013, National Defence and the Canadian Forces, and Veterans Affairs Canada will begin working together to deliver an annual report to the Deputy Ministers and Chief of the Defence Staff that updates the progress achieved against these joint priorities and establishes work for the coming year. This reporting requirement will be included in the revision of the committee's terms of reference, which is to be completed by March 2013.

Similar income support and vocational rehabilitation programs in each department continue to create confusion and difficulties

4.75 The Service Income Security Insurance Plan (SISIP) provides income support for members who are being released for medical reasons, for up to two years after release (or until the age of 65 if declared totally disabled), and vocational rehabilitation during the six months before release and up to two years after release. Veterans Affairs Canada offers vocational rehabilitation after release. While Veterans Affairs promotes intervention at the earliest stage of transition, it has expressed concern that its inability to do so could have a negative impact on the outcome of the process.

4.76 In its 2005 proposal to the government that led to the New Veterans Charter, Veterans Affairs acknowledged the issue that both departments would operate similar income support and vocational rehabilitation programs. We found that under the auspices of the joint

steering committee, between 2005 and 2009 an interdepartmental working group studied the model of a single service provider. However, in July 2009, the committee decided not to pursue this model because of the lack of support needed to advance the initiative. The committee took this decision without any analysis of the impact on Forces members who were being released. The committee also did not analyze the cost and possible inefficiencies of operating similar programs in two departments. Last, we did not see documented evidence that the joint committee reported its decision to the responsible Deputy Minister or the Chief of the Defence Staff.

4.77 Of our sample of 32 veterans who were eligible and participated in the SISIP vocational rehabilitation program, we found that 3 of them (about 9 percent) were also eligible and subsequently participated in the Veterans Affairs vocational rehabilitation program. In interviews, veterans and staff also told us that Forces members and veterans feel frustrated that they have to deal with the staff of multiple departments, submit the same documents over again, and repeat their stories before they can access benefits and services.

4.78 A SISIP annual report dated 2009 stated that the existence of two similar programs had created confusion and misunderstanding among some Forces members. The report also cited communications difficulties between staff of the two programs. In 2010, SISIP reported that the situation caused some Forces members to miss deadlines for vocational support or to act on the basis of incorrect information. Recently, SISIP reported improved communication between staff of the two programs; this is expected to reduce overlaps and confusion for Forces members being released from the military.

4.79 Finally, we found that the contract between the Canadian Forces and the private sector insurer that delivers the Service Income Security Insurance Plan dates back to 1969. Since then, it has not been subject to a competitive tendering process. As a result, there is a risk that costs are higher than necessary.

4.80 Recommendation. To inform the future direction of their respective income support and vocational rehabilitation programs, National Defence and the Canadian Forces, and Veterans Affairs Canada should conduct a joint analysis (including tracking outcomes) of the costs and benefits of each department operating similar programs.

National Defence and Canadian Forces' response. Agreed. Under the current program arrangement, Service Income Security Insurance Plan—Long Term Disability is the first provider of income support and vocational rehabilitation services for Canadian Forces members upon medical release. Veterans Affairs Canada's program provides vocational rehabilitation and income benefits to veterans who identify a service-related re-establishment need subsequent to release. This arrangement is supported by National Defence and Veterans Affairs Canada, and achieves the necessary interim alignment recommended in the Veterans Affairs Canada independent assessment of the New Veterans Charter in 2010. National Defence and the Canadian Forces will collaborate with Veterans Affairs Canada to establish, where possible, common program evaluation metrics to allow for program comparability. When sufficient data is available, the Chief of Military Personnel will consult with the Treasury Board of Canada Secretariat to review options for the future direction of the program.

Veterans Affairs Canada's response. Agreed. With the introduction of the New Veterans Charter in 2006, additional rehabilitation support became available to Canadian Forces veterans, some of whom may not previously have qualified for such support through the Service Income Security Insurance Plan—Long Term Disability. In 2013, Veterans Affairs Canada will collaborate with the Canadian Forces to explore the costs and benefits—including outcomes—of operating income support and vocational rehabilitation programs that may serve different groups of individuals but that offer similar outcomes. In undertaking this exercise, Treasury Board of Canada Secretariat guidance will be sought. The findings will inform the future direction of the two programs.

4.81 Recommendation. National Defence and the Canadian Forces should follow a competitive tendering process to select its private sector insurer.

National Defence and Canadian Forces' response. Agreed. The Chief of Military Personnel intends to obtain direction and guidance from the Chief of the Defence Staff by March 2013 on re-tendering the vocational training and long-term disability benefits program, and subsequently, to consult with the Treasury Board of Canada Secretariat to seek agreement and advice on the way ahead.

Conclusion

4.82 The Department of National Defence and the Canadian Forces, and Veterans Affairs Canada have taken some steps and have plans to address most of the issues identified in this audit. However, during the period covered by the audit (1 April 2006 to 31 March 2012), they had not taken sufficient steps to adequately manage the selected services and benefits we examined.

4.83 Both departments have difficulties in communicating and meeting service delivery standards and requirements, particularly as they relate to assessments and case management services. Problems with information sharing and data reliability also exist. In addition, both departments need to improve their performance measurement and reporting on programs and services.

4.84 An overarching governance framework has been established, with a joint steering committee to coordinate, harmonize, and communicate the various programs, services, and benefits available to ill and injured Forces members and veterans. However, this framework contains important gaps in the areas of the steering committee's mandate, the management of joint priorities, and information sharing. The existence of similar income support and vocational rehabilitation programs in each department continues to create confusion and difficulties for veterans and staff alike.

4.85 National Defence and the Canadian Forces, and Veterans Affairs Canada recognize these challenges and continue to work independently and jointly on solutions.

About the Audit

All of the audit work in this chapter was conducted in accordance with the standards for assurance engagements set by The Canadian Institute of Chartered Accountants. While the Office adopts these standards as the minimum requirement for our audits, we also draw upon the standards and practices of other disciplines.

Objective

The audit objective was to determine whether National Defence and the Canadian Forces, and Veterans Affairs Canada adequately manage selected services and benefits to support eligible ill and injured Canadian Forces members and veterans in their transition to civilian life.

For the purposes of this performance audit, adequate management of services and benefits means that National Defence and the Canadian Forces, and Veterans Affairs

- have an overarching governance structure to coordinate, harmonize, and communicate the spectrum of care, services, and benefits available to ill and injured Forces members and veterans, taking into account their assessed needs for care, treatment, and re-establishment in civilian life. That structure should also include systems and practices to identify and minimize any gaps and inefficiencies (such as overlap and duplication of departmental services and benefits), where their respective statutory and legislative mandates might allow, and to address instances of non-compliance with applicable legislation and regulations;
- have service commitments and delivery standards that are met and communicated to all Forces members and veterans, and delivery approaches that support an efficient transition and continuity of care, taking into account the assessed needs of ill and injured Forces members and veterans; and
- measure and monitor performance, act on improvement opportunities to support the transition from military life and re-establishment in civilian life, and report on performance.

Scope and approach

The audit focused on National Defence and the Canadian Forces, and Veterans Affairs Canada—the two main federal organizations responsible for managing selected federal services and benefits available to Canadian Forces members and veterans with service-related illnesses and injuries in their transition to civilian life.

The selected National Defence and Veterans Affairs services and benefits for supporting ill and injured Forces members and veterans in their transition to civilian life included

- case management services;
- mental health services and benefits;
- physical and psychosocial rehabilitation treatment services and benefits;
- vocational services and benefits;

- disability awards, and temporary and extended earnings loss financial benefits;
- transitional services provided by National Defence and the Canadian Forces to Forces members in the process of medical release, through Joint Personnel Support Units and the Integrated Personnel Support Centres;
- screening to identify and contact Forces members who are at risk of developing service-related physical and mental health problems after deployment; and
- outreach services to identify and communicate with all ill and injured Forces members and veterans in order to inform them of transition services and benefits for which they may be eligible.

The audit scope did not include an examination of whether Forces members and veterans received all benefits and services for which they were eligible. It also did not include an examination of the fairness of departmental services and benefits available to eligible Forces members and veterans, or the quality of medical treatment and care provided.

The audit approach involved reviewing selected departmental policies, systems, practices, and data, as well as other relevant documents. It also involved interviewing responsible departmental officials at headquarters and in two regions (Western and Atlantic), as well as representatives of selected veterans' organizations.

In addition, audit evidence was obtained from an examination of the records of 80 Forces members and veterans, who were randomly selected from two departmental databases:

- Canadian Forces members who were released for medical reasons between 1 April 2006 and 31 December 2011 (population = 7,705); and
- veterans who were released from the Forces between 1 April 2006 and 31 December 2011, and who became clients of the Veterans Affairs rehabilitation program in that period (population = 3,254).

The sample of 80 cases is divided as follows:

| Type of release | Veterans Affairs' rehabilitation clients | Not-Veterans' Affairs rehabilitation clients | Total |
|---------------------|--|--|--------------------------------|
| Medical release | 24 members | 30 members | 54 medical releases |
| Non-medical release | 26 members | 0 | 26 non-medical releases |
| Total | 50 Veterans Affairs' rehabilitation clients | 30 who are not Veterans Affairs' rehabilitation clients | 80 cases |

To obtain comments directly from Canadian Forces members and veterans about their transition experience, we also contacted a random sample of 100 veterans. We selected 50 veterans from each of the two databases mentioned earlier. Of these, we interviewed 25 who agreed to participate.

It is important to note that the file review and the interview samples, which were randomly selected from departmental administrative records, were not drawn as statistical samples. Therefore, caution should be exercised with regard to any statistical extrapolation to the overall populations.

Criteria

| Criteria | Sources |
|--|---|
| <p>To determine whether National Defence and the Canadian Forces, and Veterans Affairs Canada adequately manage selected services and benefits to support eligible ill and injured Canadian Forces members and veterans in their transition to civilian life, we used the following criteria:</p> | |
| <p>National Defence and the Canadian Forces, and Veterans Affairs Canada have an overarching governance structure to coordinate, harmonize, and communicate the spectrum of care, services, and benefits available to ill or injured Forces members and veterans, taking into account their assessed needs for care, treatment, and re-establishment in civilian life.</p> | <ul style="list-style-type: none"> • <i>Federal Accountability Act</i> • <i>Canadian Forces Members and Veterans Re-establishment and Compensation Act</i> • <i>Veterans Health Care Regulations</i> • Management Accountability Framework, Treasury Board of Canada Secretariat • Veterans Affairs Canada Service and Program Modernization Task Force, Principles and Policy Directives, 2004 • Five-Year Strategic Plan 2009–14, Veterans Affairs Canada • 2010–11 Report on Plans and Priorities, Veterans Affairs Canada • Departmental Performance Report 2010–11, National Defence |
| <p>National Defence and the Canadian Forces, and Veterans Affairs Canada have systems and practices to identify and minimize any gaps and inefficiencies (such as overlap and duplication of departmental services and benefits), where their respective statutory and legislative mandates might allow, and to address instances of non-compliance with applicable legislation and regulations.</p> | <ul style="list-style-type: none"> • Companion Guide—The Development of Results-based Management and Accountability Frameworks for Horizontal Initiatives, Treasury Board of Canada Secretariat • Policy on Transfer Payments, Treasury Board, 2008 |
| <p>National Defence and the Canadian Forces, and Veterans Affairs Canada have service commitments and delivery standards that are met and communicated to all Forces members and veterans, and delivery approaches that support an efficient transition and continuity of care, taking into account the assessed needs of ill and injured Forces members and veterans.</p> | <ul style="list-style-type: none"> • Communications Policy of the Government of Canada, Treasury Board, 2006 • Management Accountability Framework, Treasury Board of Canada Secretariat • Veterans Bill of Rights, 2007 • Veterans Affairs Canada Service and Program Modernization Task Force, Principles and Policy Directives, 2004 • Five-Year Strategic Plan 2009–14, Veterans Affairs Canada • 2010–11 Report on Plans and Priorities, Veterans Affairs Canada • Military Human Resources Strategy 2020, National Defence • Case Management Vision, Canadian Forces • Departmental Performance Report 2010–11, National Defence |
| <p>National Defence and the Canadian Forces, and Veterans Affairs Canada measure and monitor performance, act on improvement opportunities to support the transition from military life and re-establishment in civilian life, and report on performance.</p> | <ul style="list-style-type: none"> • Policy on Management, Resources and Results Structures, Treasury Board, 2010 • Policy on Evaluation, Treasury Board, 2009 • Statement of Recommended Practice (SORP-2), Public Performance Reporting, Public Sector Accounting Board, 2006 |

The management of National Defence and the Canadian Forces, and Veterans Affairs Canada reviewed and accepted the suitability of the criteria used in the audit.

Period covered by the audit

The audit covered the period from 1 April 2006 to 31 March 2012, including any significant subsequent events up to the date of the audit report. Audit work for this chapter was completed on 17 July 2012.

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Appendix List of recommendations

The following is a list of recommendations found in Chapter 4. The number in front of the recommendation indicates the paragraph where it appears in the chapter. The numbers in parentheses indicate the paragraphs where the topic is discussed.

| Recommendation | Response |
|---|---|
| <p>Service delivery</p> <p>4.23 National Defence and the Canadian Forces, and Veterans Affairs Canada should streamline and automate their transition policies and administrative processes to make it easier for ill and injured Forces members and veterans to access programs and benefits in a timely manner. (4.18–4.22)</p> | <p>National Defence and Canadian Forces' response. Agreed. The recently published document, <i>Caring For Our Own: A comprehensive approach for the care of CF ill and injured members and their families</i>, and the regularly updated booklet, <i>Death and Disability Benefits, Programs and Services: A Guide for Serving and Former Canadian Forces Personnel and Their Families</i>, are illustrative of our efforts in consolidating policy and procedural information and communicating it in non-technical terms. In collaboration with Veterans Affairs Canada, National Defence and the Canadian Forces will continue to streamline and, where practical, automate transition policies and administrative processes.</p> <p>Veterans Affairs Canada's response. Agreed. Veterans have told us they want a more hassle-free system, and the Department is committed to delivering this. Through the Transformation Agenda, all programs, policies, and business processes are under review. Measures to cut red tape, overhaul service delivery, and improve technology platforms mean that veterans and their families will get faster, one-stop access to information and support when they need it and for as long as they need it. For example:</p> <ul style="list-style-type: none"> • Veterans now can visit any of Service Canada's 600 points of service for information on programs or help applying for benefits. • Some 80 percent of calls to the Department are answered within two minutes. • Benefits are being delivered faster. Most disability applications are processed within 16 weeks, 30 percent faster than before. Most rehabilitation applications are processed in two weeks or less, 50 percent faster than before. • More avenues have been identified to support homeless veterans. |

Recommendation**Response**

By March 2013, the Department will do the following:

- review, revise, and reduce the number of policies guiding the delivery of benefits. Policies will offer clear, modern-day solutions to veterans' needs, and will foster greater harmony related to the spectrum of health care benefits available to serving and released Canadian Forces members;
- better streamline and coordinate services through each of the 24 Integrated Personnel Support Centres so that injured and ill Canadian Forces members and veterans have faster, more seamless access to the benefits they need;
- make it easier for individuals to be referred to the network of mental health clinics operated by Veterans Affairs Canada and National Defence; and
- further improve turnaround times to 12 weeks for disability benefit decisions.

4.24 National Defence and the Canadian Forces, and Veterans Affairs Canada should continue to simplify the language that explains the support available to ill and injured Forces members and veterans. They should ensure that information is updated and communicated to staff and potential beneficiaries, as appropriate, using online tools such as the Benefits Browser. (4.17–4.22)

National Defence and Canadian Forces' response. Agreed. National Defence and the Canadian Forces are taking action to address this recommendation. A new, user-friendly website designed to communicate information on benefits and programs in clear and concise language is under development. We will undertake a review during 2013 of pamphlets, information booklets, and other hard-copy materials made available to Canadian Forces members and their families to ensure that information on benefits and programs is up to date and understandable. Additionally, the outreach briefings provided to Regular and Reserve Force units will be reviewed for currency and clarity. The feasibility and resource implications of including formal readability reviews as part of the development process for any new information tools will also be investigated during 2013.

Veterans Affairs Canada's response. Agreed. Veterans Affairs Canada believes veterans have the right to access information that is clear and easy to understand. As part of the Department's ongoing commitment to reach out to veterans and their families:

- Work has accelerated to simplify disability benefit decision letters, as well as decision letters related to health care and home care benefits. This builds on work that began in 2009.

Recommendation**Response**

- By March 2013, veterans and their families will find it easier to apply online for benefits and navigate the website with the help of a new Benefits Browser that simplifies the process of gathering information about programs and policies.
- A similar type of Benefits Browser already is being used internally by staff to help them access relevant information online to serve veterans more quickly.
- Work is well under way to simplify forms and minimize the amount of paperwork that veterans and families must submit.
- In cooperation with National Defence, the Canadian Forces, and other service partners, the Department also will continue to attend events and information sessions across the country to share clear information on benefits and services with veterans, still-serving personnel, and their families.

4.28 National Defence and the Canadian Forces, and Veterans Affairs Canada should ensure that their databases contain reliable data about Forces members, and that Canadian Forces and Veterans Affairs processes are managed to facilitate the timely and efficient sharing of authorized information. (4.25–4.27)

National Defence and Canadian Forces' response. Agreed. In close cooperation with Veterans Affairs Canada, National Defence and the Canadian Forces will continue to improve business processes and implement new tools to facilitate the maintenance of accurate information and the timely and efficient sharing of such information. The primary Canadian Forces database for casualty administration is the Mission Support System. It is currently being upgraded and is expected to be rolled out in early 2013. In the area of medical information, Veterans Affairs Canada and the Canadian Forces currently have a joint project under way that will enable the disclosure of Canadian Forces members' personal health information to Veterans Affairs Canada in a more efficient, centralized, and trackable way. The intent is to conduct pilot tests in fall 2012, and undertake nationwide implementation in 2013. Methods for ensuring database accuracy will be reviewed as integral elements of these programs.

Veterans Affairs Canada's response. Agreed. Sharing information internally and with the Canadian Forces through a secure electronic environment is a key initiative under the Department's Transformation Agenda.

- In 2012, the Canadian Forces service number that individuals receive when they join the military has become the standard way to identify those who later apply for departmental

Recommendation**Response**

4.33 National Defence and the Canadian Forces, and Veterans Affairs Canada should develop and implement policies and processes for coordinating the delivery of services to Forces members and veterans at the Integrated Personnel Support Centres.

(4.29–4.32)

benefits. This will make it easier to track the benefits and services veterans receive over their lifetime, leading to better continuity of care, accurate information sharing, and better privacy safeguards.

- The switch to electronic records already is under way. To date, more than two million pages of veterans' files have been scanned.
- In July 2012, the electronic transfer of still-serving members' files began at two Canadian Forces bases. Already, the positive results from these pilots suggest that the national rollout to another 21 bases may conclude well ahead of the scheduled completion date of 2015.
- By 2015, or before, the time to transfer records will drop from seven weeks to one week, further accelerating the decision-making process so that veterans receive faster access to benefits.

National Defence and Canadian Force's response. Agreed. The requirement to develop integrated transition plans was announced on 11 October 2011. Guidance was issued, via a Canadian Forces directive, on 30 October 2011, to assist all Integrated Personnel Support Centres in developing integrated transition plans for their clients. Business processes and standard operating procedures in this area have been, and will continue to be, reviewed, standardized, and implemented as the Joint Personnel Support Unit framework evolves, with a target date of December 2013 for completion of this effort.

Veterans Affairs Canada's response. Agreed. Already, staff from Veterans Affairs Canada, National Defence, and the Canadian Forces work side by side to support up to 1,300 injured and other Forces members and veterans who contact the national network of 24 Integrated Personnel Support Centres each month.

Operational guidelines for the centres are already in place. As of October 2011, integrated transition plans are offered to all severely injured and ill personnel, although not all accept the offer. The role of the Veterans Affairs case manager is well established in this process.

Recommendation**Response**

4.40 National Defence and the Canadian Forces should develop and communicate service standards for the decision on employment limitations for medical reasons and the decision on medical release. (4.37–4.39)

4.41 In consultation with Veterans Affairs Canada, National Defence and the Canadian Forces should evaluate how the new Career Transition Support Policy affects ill and injured members' reintegration into civilian life. (4.37–4.39)

Since the first centres were launched in 2009, all partners have learned a great deal about how best to support those who are injured and ill. In 2013, the best practices that have been developed will be used to fully implement a set of common business processes and practices across the network of centres. This will further streamline and coordinate the delivery of programs and services to all those who seek support.

National Defence and Canadian Forces' response. Agreed. Since May 2012, the Director of Military Careers Administration has been engaged in a complete review of the efficiency, effectiveness, and service delivery of administrative procedures. This will enhance the ability of the Canadian Forces to complete administrative reviews and to render decisions within improved timelines. While taking into consideration the average volume of files to be considered, essential procedural requirements, and staff resources available, National Defence and the Canadian Forces undertake to review, by March 2013, the feasibility of establishing service standards for typical non-complex cases, for both the medical employment limitation decision process and the medical release review process.

National Defence and Canadian Forces' response. Agreed. The provision of a seamless transition between partnering organizations, through improved communication and co-location, is one of the objectives identified in the Joint Personnel Support Unit performance measurement framework. This framework will be further developed to ensure that we are able to assess whether the new transition policy is in fact meeting the requirements of our ill and injured personnel. Once the Mission Support System rollout is completed (current estimate is early 2013), the Canadian Forces and National Defence will be able to develop indicators of transition readiness, and in collaboration with Veterans Affairs Canada, will attempt to capture post-release information on how the Career Transition Support Policy affects reintegration into civilian life.

Veterans Affairs Canada's response. Agreed. Up to six months before release, Veterans Affairs case managers, in collaboration with National Defence and the Canadian Forces, help Forces members who are being released to access services. This early

Recommendation**Response**

intervention gives members and their families the ability to transition from the military to civilian life as seamlessly as possible. Once they are released, veterans may qualify for Veterans Affairs Canada's Rehabilitation Program, where the focus is on assessing their needs, rehabilitating them to the fullest extent possible, and then linking them with vocational rehabilitation experts who can help them prepare for a meaningful civilian career.

Veterans Affairs Canada also is working with the business community and various not-for-profit organizations to create more employment opportunities for Forces members who are being released and former Forces members.

Veterans Affairs Canada will continue to assist and support National Defence and the Canadian Forces, as appropriate, in their efforts to further assess if the Career Transition Support Policy is, in fact, meeting the requirements of ill and injured personnel.

4.53 Veterans Affairs Canada should clarify and communicate the roles and responsibilities of all parties involved in the case management service. It should develop and implement a department-wide quality management system for this service. (4.42–4.52)

Veterans Affairs Canada's response. Agreed. The ability to monitor and measure the success of the case management function is a priority for the Department and a cornerstone of the Transformation Agenda. To strengthen support to veterans with more complex needs:

- Roles and responsibilities have been clarified for Veterans Affairs' client service team members. As business processes and veterans' needs evolve, roles and responsibilities will continue to be adjusted and communicated to all those involved in the case management process.
- Veterans enrolled in the Rehabilitation Program have faster access to benefits that are part of their case plan now that case managers have been empowered to make more decisions without additional approvals.
- Processes and standards are in place to give all case-managed veterans more access to their case manager.
- National training and learning tools are in place, and more are planned for 2012–13.
- National monitoring processes will be reviewed and adjusted, as needed, to continue to ensure that case management is delivered as intended.

Recommendation**Response****Performance measurement and reporting**

4.57 National Defence and the Canadian Forces should maintain consolidated information on ill and injured Forces members who will be released for medical reasons to help better manage programs and services to support their transition. (4.55–4.56)

4.59 National Defence and the Canadian Forces, in cooperation with Veterans Affairs Canada, should continue to improve management of its support for the transition to Veterans Affairs Canada of ill and injured Forces members, particularly reservists. (4.58)

National Defence and Canadian Forces' response. Agreed. The Canadian Forces remain committed to ensuring our programs and services are meeting the needs of our ill and injured Forces members. The Joint Personnel Support Unit's performance measurement framework will continue to be used as the blueprint for the measurement, evaluation, and reporting of program and service performance. Surveys administered to Joint Personnel Support Unit clients and the local chain of command will be used to assess the utility of programs and services from a user perspective. There are also a number of projects under way that are designed to improve the consolidation of personal health information, in accordance with the *Privacy Act*, as well as a project to ensure that all Reserve documents are available electronically in the Canadian Forces Health Information System by the end of 2012. A new policy mandating that all new forms go through a standardized approval process to prevent the proliferation of separate systems and non-standardized forms is expected by fall 2012. Finally, a quality assurance program is now being developed for rollout at the local level, with headquarters oversight and guidance, in 2013.

National Defence and Canadian Forces' response. Agreed. While recognizing that Canadian Forces responsibility for follow-up formally ends when a member is released, ill and injured members will be tracked by the Canadian Forces until an individual returns to unrestricted duty; a former Canadian Forces member (including reservists) is able to resume or seek employment; a member is able to cope independently without any further assistance; or a member expresses that he or she no longer wishes any further contact. By June 2013, the Canadian Forces and National Defence will review procedures to ensure that, when required or appropriate, members who are being released for medical reasons, especially reservists, successfully make the transition to Veterans Affairs Canada care. In partnership with Veterans Affairs Canada, the Canadian Forces and National Defence will, also by June 2013, examine options to improve systematic post-release follow-up.

Recommendation**Response**

Veterans Affairs Canada's response. Agreed. In collaboration with National Defence and the Canadian Forces, work is ongoing to

- provide ill or injured members with immediate and ongoing support through all stages of recovery, rehabilitation, and reintegration into civilian life;
- offer transition interviews to Regular and Reserve Force members who are being released, and their families, and encourage them to attend; and
- provide members who are being released for medical reasons or those who have not been able to make a successful transition with timely access to Veterans Affairs Canada's Rehabilitation Program.

In 2013, the Department

- will collaborate with National Defence and the Canadian Forces to examine options to further improve systematic post-release follow-up; and
- in collaboration with National Defence and the Canadian Forces, will partner with Statistics Canada to conduct research on the transition experience of former reservists. This is a follow-up to the 2011 Life After Service Study, which included an increased focus on reservists in addition to Regular Force veterans. Going forward, these research findings will add to the Department's understanding of how to design, implement, and deliver policies, programs, and business processes that best meet the needs of ill and injured personnel, including reservists.

4.62 Veterans Affairs Canada should publicly communicate performance against service standards. (4.60–4.61)

Veterans Affairs Canada's response. Agreed. By May 2013, the Department will formally post its performance against all published service standards for the 2012–13 fiscal year on the Department's website. These results will be updated every year.

4.66 Veterans Affairs Canada should improve its client and expenditure forecasting for the New Veterans Charter programs. (4.63–4.65)

Veterans Affairs Canada's response. Agreed. As part of the action plan to improve the accuracy of client and expenditure forecasting, the Department will continue to

- expand partnerships and consultation with National Defence and the Canadian Forces to source all possible data relevant to forecasting methodologies;

Recommendation**Response**

- validate forecasting assumptions and methodologies through an independent third party; and
- continue to partner with National Defence, the Canadian Forces, and Statistics Canada on a series of research projects to better understand the transition experience of both Regular and Reserve Force members. This follow-up to the 2011 Life After Service Study will include data on the overall veteran population, not just those who receive departmental benefits, allowing for a broader understanding of veterans' health and wellness over their lifetime. In addition, the current study will place increased emphasis on reservists, a group making up about 50 percent of Canada's overall population of veterans.

Governance and coordination

4.73 National Defence and the Canadian Forces, and Veterans Affairs Canada should update the joint steering committee's terms of reference to specify its authority, responsibility, and accountability. (4.69–4.72)

National Defence and Canadian Forces', and Veterans Affairs Canada's response. Agreed. By March 2013, National Defence and the Canadian Forces, and Veterans Affairs Canada will update the terms of reference for the committee to ensure a clear delineation of committee authority, responsibility, and accountability.

4.74 For each approved joint priority, the steering committee should establish measurable objectives and specific timelines for completion. It should prepare an annual report to the Deputy Ministers and the Chief of the Defence Staff, summarizing progress achieved against the joint priorities. (4.69–4.72)

National Defence and Canadian Forces', and Veterans Affairs Canada's response. Agreed. In 2011, the joint steering committee identified objectives and timelines for seven priorities: continuity of care; transition management; transfer of electronic Canadian Forces personnel records; a joint mental health strategy; outreach, consultation and engagement; commemoration; and research. These priorities continue to evolve as progress is achieved and new plans are developed.

In 2013, National Defence and the Canadian Forces, and Veterans Affairs Canada will begin working together to deliver an annual report to the Deputy Ministers and Chief of the Defence Staff that updates the progress achieved against these joint priorities and establishes work for the coming year. This reporting requirement will be included in the revision of the committee's terms of reference, which is to be completed by March 2013.

Recommendation**Response**

4.80 To inform the future direction of their respective income support and vocational rehabilitation programs, National Defence and the Canadian Forces, and Veterans Affairs Canada should conduct a joint analysis (including tracking outcomes) of the costs and benefits of each department operating similar programs. (4.75–4.79)

National Defence and Canadian Forces' response. Agreed. Under the current program arrangement, Service Income Security Insurance Plan—Long Term Disability is the first provider of income support and vocational rehabilitation services for Canadian Forces members upon medical release. Veterans Affairs Canada's program provides vocational rehabilitation and income benefits to veterans who identify a service-related re-establishment need subsequent to release. This arrangement is supported by National Defence and Veterans Affairs Canada, and achieves the necessary interim alignment recommended in the Veterans Affairs Canada independent assessment of the New Veterans Charter in 2010. National Defence and the Canadian Forces will collaborate with Veterans Affairs Canada to establish, where possible, common program evaluation metrics to allow for program comparability. When sufficient data is available, the Chief of Military Personnel will consult with the Treasury Board of Canada Secretariat to review options for the future direction of the program.

Veterans Affairs Canada's response. Agreed. With the introduction of the New Veterans Charter in 2006, additional rehabilitation support became available to Canadian Forces veterans, some of whom may not previously have qualified for such support through the Service Income Security Insurance Plan—Long Term Disability. In 2013, Veterans Affairs Canada will collaborate with the Canadian Forces to explore the costs and benefits—including outcomes—of operating income support and vocational rehabilitation programs that may serve different groups of individuals but that offer similar outcomes. In undertaking this exercise, Treasury Board of Canada Secretariat guidance will be sought. The findings will inform the future direction of the two programs.

4.81 National Defence and the Canadian Forces should follow a competitive tendering process to select its private sector insurer. (4.75–4.79)

National Defence and Canadian Forces' response. Agreed. The Chief of Military Personnel intends to obtain direction and guidance from the Chief of the Defence Staff by March 2013 on re-tendering the vocational training and long-term disability benefits program, and subsequently, to consult with the Treasury Board of Canada Secretariat to seek agreement and advice on the way ahead.

Report of the Auditor General of Canada to the House of Commons

Matters of Special Importance

Main Points—Chapters 1 to 7

Appendices

Planning the Use of Professional Service Contractors

Grant and Contribution Program Reforms

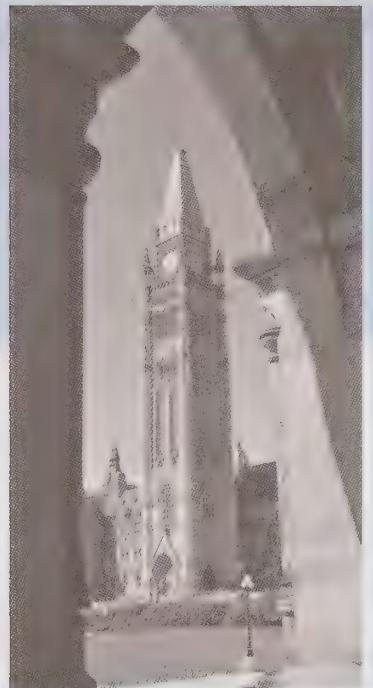
Protecting Canadian Critical Infrastructure Against Cyber Threats

Transition of Ill and Injured Military Personnel to Civilian Life

Real Property—National Defence

Transfer Payments to the Aerospace Sector—Industry Canada

Long-Term Fiscal Sustainability—Finance Canada



Report of the Auditor General of Canada to the House of Commons

Real Property—National Defence



Office of the Auditor General of Canada

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Report of the Auditor General of Canada to the House of Commons

CHAPTER 5 Real Property—National Defence



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CHAPTER 5

Real Property—National Defence



Performance audit reports

This report presents the results of a performance audit conducted by the Office of the Auditor General of Canada under the authority of the *Auditor General Act*.

A performance audit is an independent, objective, and systematic assessment of how well government is managing its activities, responsibilities, and resources. Audit topics are selected based on their significance. While the Office may comment on policy implementation in a performance audit, it does not comment on the merits of a policy.

Performance audits are planned, performed, and reported in accordance with professional auditing standards and Office policies. They are conducted by qualified auditors who

- establish audit objectives and criteria for the assessment of performance;
- gather the evidence necessary to assess performance against the criteria;
- report both positive and negative findings;
- conclude against the established audit objectives; and
- make recommendations for improvement when there are significant differences between criteria and assessed performance.

Performance audits contribute to a public service that is ethical and effective and a government that is accountable to Parliament and Canadians.

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Real Property—National Defence

Main Points

What we examined

The Department of National Defence's real property includes lands, some 20,000 buildings, and over 13,000 works in installations and bases across Canada. Buildings can include armouries and barracks, storage and maintenance facilities, and hangars. Works are divided between service works such as roads, sewers, and fuel tanks, and operational works such as airfields, docks, and firing ranges. This infrastructure provides critical support to operations. It is used to sustain military personnel, provide training facilities, store and protect essential material, and deploy forces.

We examined whether National Defence has exercised sound stewardship in managing its real property. Audit work focused on the systems and practices used to deliver infrastructure at 21 main bases at which forces are organized, trained, and equipped and from which they are rapidly deployed. Residential housing was excluded from the scope of the audit.

Audit work for this chapter was completed on 17 July 2012. More details on the conduct of the audit are provided in **About the Audit** at the end of the chapter.

Why it's important

Real property infrastructure is essential to the Canadian Forces' ability to undertake core missions in Canada and abroad. It is one of four pillars of the Government's 2008 *Canada First* Defence Strategy to build an effective military. The strategy commits to spending \$40 billion over 20 years, or 8 percent of all defence spending, on maintaining and renewing the Department's real property.

National Defence reported in 2010 a steady decline of the condition of its real property infrastructure since the 1990s. According to the Department, 43 percent of its non-residential buildings and 61 percent of works were over 50 years old. Older infrastructure is typically less suited to serve current needs and, when not maintained in good condition, it carries increased risks of operational failure or risks to health and safety. Given the size, complexity, and extent of National Defence's portfolio and its critical impact on the Canadian Forces' operational capabilities, it is important that it be managed accordingly.

What we found

- National Defence has not yet put in place a real property management framework or national strategy for managing real property. Both have been drafted but neither has been approved and issued. The draft strategy lays out a roadmap to achieve stewardship, including a new portfolio management approach, stewardship reporting, integrated real property management, a new performance management and reporting framework, updated information systems, and risk-based investment planning. The framework requires master real property development plans at the bases and a national master real property development plan. Some of these elements are in place but until the strategy, framework, and a national master real property development plan are complete, the Department cannot know if it has the required real property assets at the right place, at the right time, to meet the operational requirements of the Canadian Forces.
- There are gaps in National Defence's management practices for acquiring, maintaining, and repairing capital assets. Headquarters have not provided bases with performance objectives and targets for important performance indicators such as indices of condition or suitability of real property. The overall performance management framework for real property is incomplete and headquarters do not have the information they need to assess the condition of real property assets. The Department's approval process for construction projects is cumbersome and lengthy. Planning and delivery of important projects takes about six years. Preventive maintenance practices are insufficient. The focus is often on maintenance after breakdown, resulting in a premature failure of real property assets. Many locations were found to not be compliant with the National Fire Code of Canada. For example, required inspections of fire alarms were often not being conducted. There were instances of non-compliance with other health and safety requirements. This means that the health and safety of workers in the affected facilities could be at risk.
- National Defence has been unable to meet its expenditure targets for maintenance and repair and recapitalization. Bases often do not receive funds for maintenance and repair and recapitalization early enough in the fiscal year to match plans and projects with the construction cycle. The Department reports that its inability to meet targets is due in part to a lack of personnel but it cannot expect significantly more human resources. National Defence will have to transform the way it manages real property to fulfill all the requirements of sound stewardship.

The Department has responded. National Defence agrees with all of the recommendations. Its detailed responses follow the recommendations throughout the chapter.

Introduction

5.1 Real property infrastructure is essential to the Canadian Forces' ability to undertake its core missions in Canada and abroad. This infrastructure supports operations and training, accommodates personnel and stores, protects essential material, and enables forces to deploy. Failure to match infrastructure investment with operational needs risks lowering the Canadian Forces' ability to organize, train, equip, and rapidly deploy forces.

5.2 Real property infrastructure is made up of works, buildings, and lands, including ranges and training areas. National Defence land holdings include approximately 2.3 million hectares, of which over 900,000 hectares is leased from the provinces. Holdings incorporate over 20,000 buildings and 13,000 works concentrated among 23 bases across Canada as well as smaller sites in every province and territory. Typical buildings include administration buildings, ammunition bunkers, armouries, barracks, health service centres, hangars, and storage and maintenance facilities. Works are divided between service works, such as roads and sewers, and operational works, such as fuelling stations, airfields, docks, weapons firing ranges, and training areas.

5.3 In 2010, National Defence reported that budget cuts in the 1990s resulted in much of its infrastructure aging and being in need of refurbishment or repair. The Department also reported that 43 percent of its non-residential buildings and 61 percent of its works were over 50 years old. The Department determined that between 2001 and 2008, the condition of its non-residential buildings deteriorated by 6 percent while the condition of its works declined by 15 percent. Old infrastructure is generally less suitable for current needs, and when it is not maintained in good condition, it increases the risks of failure or risks to health and safety.

5.4 The government approved the 2008 *Canada First Defence Strategy* to build an effective military. The strategy identifies real property as one of the four main pillars needed to succeed. From the 2008–09 fiscal year to the 2027–28 fiscal year, the strategy commits spending of \$40 billion on real property, including expenditures on new construction, **recapitalization**, and maintenance and repair. This amounts to 8 percent of the estimated total of \$490 billion that will be spent on defence in that 20-year period.

Base—A military installation that operates under a single command and is composed of land, buildings, and works at one or more locations. The Royal Canadian Air Force calls its bases “wings.”

Recapitalization—The investment to replace existing real property in order to meet regulatory requirements or expenditures for improvements such as increased service capacity or extension of its useful life.

Departmental real property management responsibilities

5.5 National Defence's Deputy Minister is accountable to the Minister of National Defence and to the Treasury Board for the sound stewardship of the Department's real property. Since 1995, National Defence has divided real property management responsibilities between functional authority and custodial authority. The functional authority is the Assistant Deputy Minister (Infrastructure and Environment), who is accountable to the Deputy Minister. The Assistant Deputy Minister (Infrastructure and Environment) works outside the military chain of command, and is responsible for

- providing functional direction, guidance, and oversight of the real property activities, on behalf of the Deputy Minister;
- leading and coordinating real property activities to ensure the stewardship of the Department's portfolio;
- establishing national strategies, plans, and guidance for the entire real property portfolio;
- developing the infrastructure component of the Department's annual plan for investing in assets (the Capital Investment Plan); and
- managing projects estimated to cost over \$1 million.

5.6 The major custodial authorities are the Chief Military Personnel, and the commanders of the Royal Canadian Navy, the Canadian Army, and the Royal Canadian Air Force. They operate within the military chain of command, are directly accountable to the Chief of the Defence Staff, and are responsible for

- following functional guidance provided by the Department;
- identifying and assessing operational requirements;
- planning portfolio development to identify how and where development should take place;
- establishing investment priorities and assigning resources;
- conducting life-cycle planning for maintenance, repair, or recapitalization;
- delivering facilities maintenance and repair services;
- managing capital projects under \$1 million and those authorized by the Assistant Deputy Minister (Infrastructure and Environment) under \$5 million; and
- complying with health and safety requirements.

5.7 The Chief Military Personnel and the commanders of the Navy, the Army, and the Air Force normally delegate their custodial responsibility and allocate funds to base commanders. In most cases, the base commander is supported by a base construction engineering organization. Base commanders are responsible for

- conducting life-cycle and development planning activities at the base,
- recommending investment priorities to the major custodians,
- managing projects under \$1 million delegated by the major custodians,
- overseeing day-to-day real property management practices at the base, and
- establishing monitoring and compliance programs for health and safety at the base.

5.8 While leasing and purchasing is typically contracted through Public Works and Government Services Canada, Defence Construction Canada is the contracting authority for all infrastructure projects costing more than \$60,000. Defence Construction Canada is a Crown corporation accountable to Parliament through the Minister of Public Works and Government Services Canada. Created in 1951, its sole client is National Defence.

5.9 National Defence employs approximately 5,000 people to manage, operate, and maintain real property. Its military and civilian workforce consists of engineers, architects, tradespeople, general labourers, geographic information system technicians, urban planners, economists, and analysts, among others.

Focus of the audit

5.10 Our audit objective was to determine whether National Defence has exercised sound stewardship in managing its real property. We examined whether the Department has a real property management framework as well as master real property development plans for the Department and bases. We examined how the Department manages its real property infrastructure. We did this by determining whether National Defence has clearly defined, budgeted, and communicated future and present real property needs to bases, and whether the Department has provided new infrastructure and carried out recapitalization to bases according to Treasury Board requirements.

Finally, we examined how the Department spends its real property funding and allocates human resources in support of real property. We did not examine residential housing. More details about the audit objectives, scope, approach, and criteria are in **About the Audit** at the end of this chapter.

Observations and Recommendations

Planning for real property needs

5.11 The Treasury Board requires departments that manage real property for the government to develop a real property management framework. This framework integrates real property with other departmental resources to meet operational needs. Such a framework should set out a comprehensive, cohesive, and coherent approach to managing a department's real property in support of its programs. Departments must manage their investments in real property as a portfolio rather than as individual assets.

5.12 We examined whether National Defence has a framework for managing real property as well as master plans for developing real property for the Department and bases. The framework and development plans should define the Department's real property needed to support military activities. We analyzed the planning activities at headquarters and the plans at the 21 main bases responsible for organizing, training, equipping, and rapidly deploying forces.

National Defence has not yet completed its real property planning framework

5.13 We found that National Defence does not yet have a real property management framework in place. In response to the Treasury Board requirement for a real property management framework, the Department has drafted but not yet put in place a document entitled Real Property Management Framework, dated November 2010. The framework was drafted to meet the Treasury Board requirement and to help implement the Department's own real property strategy (see paragraph 5.16). Among other priorities, the draft framework stated a need to make definitive progress on master real property development plans.

5.14 In 2010, the Assistant Deputy Minister (Infrastructure and Environment) advised custodians to have base-level master real property development plans prepared. These plans are to provide a 20-year forecast of the development of buildings, works, lands, ranges, and training areas. They are intended to guide development

decisions so that bases grow in a safe, secure, suitable, and sustainable manner to meet future operational priorities. These plans will provide input into planning for capital projects, including projects in the Department's Capital Investment Plan (Infrastructure). The plans will also contribute to the drafting of a national master real property development plan.

5.15 We found that 18 of the 21 bases now have current master real property development plans. Twelve of the 18 completed plans met the Department's guidelines. The other 6 completed plans were missing various required elements, such as background information, the evaluation of the present condition of real property, or the evaluation of challenges and opportunities. National Defence has not yet incorporated base master real property development plans into a national master real property development plan.

5.16 In addition, National Defence has drafted, but has not implemented, an overarching document intended to deal with all matters relating to its real property portfolio. The document, dated November 2010, is entitled Defence Real Property Strategy. The strategy sets out a roadmap to provide the right assets, in the right place at the right time. Essential elements include

- a new approach to real property portfolio management,
- production of a real property stewardship report,
- integrated real property management,
- risk-based investment planning,
- a new real property performance management and reporting framework, and
- new technology to transform the provision of infrastructure as well as related services.

5.17 Most of the requirements set out in the Real Property Strategy are not in place. However, National Defence has put in place risk-based investment planning. This is done through the Department's national annual Capital Investment Plan (Infrastructure). The Capital Investment Plan (Infrastructure) is required by Treasury Board and includes infrastructure investments greater than \$1 million over the next 10 years. Its main purpose is to identify funding and requirements for individual assets that have been identified at various levels in the chain of command to support Canadian Forces activities.

5.18 Until National Defence completes development and fully implements its Real Property Strategy, Real Property Management Framework, and national master real property development plan, it cannot know if it has the right assets, in the right place at the right time, to meet the operational requirements of the Canadian Forces.

5.19 Recommendation. National Defence should complete development of and implement its Real Property Strategy, Real Property Management Framework, and national master real property development plan.

The Department's response. Agreed. National Defence, through the Infrastructure and Environment Transformation Initiative, is taking all necessary actions to complete the development and implementation of its Real Property Strategy and Real Property Management Framework. The development of the National Real Property Development Plan is under way and will be coordinated with the Department's investment planning cycle.

Real property management practices

5.20 We examined National Defence's real property management practices to determine whether the Department

- acquired new infrastructure and carried out recapitalization projects according to planned timelines and costs,
- implemented effective risk management and controls to manage its infrastructure projects delivered by Defence Construction Canada,
- managed performance and monitored requirements for maintaining real property for operations,
- implemented preventive maintenance practices, and
- ensured infrastructure does not present hazards or risks to the health or safety of personnel.

Project approval processes are cumbersome and lengthy

5.21 National Defence splits its capital program into minor projects that cost less than \$5 million and major projects that cost more than \$5 million. Depending on the Department's risk assessment, real property capital projects estimated to cost more than \$5 million must either be sent to the Minister or to the Treasury Board for approval. The Assistant Deputy Minister (Infrastructure and Environment) approves projects between \$1 million and \$5 million. In practice, base commanders approve real property capital projects of \$1 million or less and these are not included in National Defence's capital investment

planning process. A 2011 evaluation by National Defence of its real property acquisition, maintenance, and disposal program noted that with increased costs for building materials and labour, the approval level of \$1 million by base commanders has become restrictive.

5.22 Once a project is approved, Defence Construction Canada is the contract authority for managing the construction phase for all projects estimated to cost \$60,000 or more. Projects estimated to cost less than \$60,000 may be procured through an existing Government of Canada standing offer or be put out to tender by either Public Works and Government Services Canada or the base.

5.23 Construction projects should be completed on time and on budget. We examined whether new capital and recapitalization projects at bases were completed within planned timelines and costs. We interviewed senior employees and examined documents concerning timely approval of planned projects.

5.24 We examined 49 projects that were completed between April 2010 and September 2011. This consisted of all 8 projects that cost over \$5 million, a sample of 4 projects that cost between \$1 million and \$5 million, and a sample of 37 projects that cost less than \$1 million.

5.25 We tested the 12 projects costing over \$1 million for time and cost overruns and how the cost and time overruns may have related to each other. As our points of reference for time, we used the earliest documented estimated completion date. We noted that timelines were often re-established before the final approval and as the project advanced to completion. For cost, we compared cost estimates at initial project identification, at project approval, and at final delivery.

5.26 We found that 7 of these 12 projects over \$1 million lacked initial project documentation. However, we were able to compare initial cost estimates, estimates put forward for final project approval, and final delivered costs for 5 projects. Based on initial cost estimates, the Department delivered 2 projects below the estimate and 3 over the estimate. For these 5 projects, we found no consistent relationship between time to complete a project and any project cost overrun.

5.27 We found that all the projects costing more than \$1 million were delivered at least 10 months later than planned, with 1 more than 5 years later (Exhibit 5.1). We also found that the average time to complete the 8 projects costing more than \$5 million was about 6 years.

Exhibit 5.1 All projects over \$1 million exceeded target completion date by at least 10 months

| Projects examined | Project's initial delivery target (in months) | Project's actual delivery time (in months) | Number of months late (past target) |
|-------------------|---|--|-------------------------------------|
| 1 | 19 | 29 | 10 |
| 2 | 8 | 20 | 12 |
| 3 | 12 | 25 | 13 |
| 4 | 12 | 25 | 13 |
| 5 | 59 | 73 | 14 |
| 6 | 12 | 29 | 17 |
| 7 | 29 | 55 | 26 |
| 8 | 53 | 85 | 32 |
| 9 | 49 | 97 | 48 |
| 10 | 49 | 100 | 51 |
| 11 | 29 | 86 | 57 |
| 12 | 50 | 113 | 63 |

Source: National Defence data

5.28 Capital projects estimated to cost less than \$1 million are usually planned and delivered by the base. We found that 33 of the 37 sampled projects that cost less than \$1 million were under base control. These follow less detailed planning and approval procedures. In order to determine time overruns for these projects, we examined the earliest project documentation available, such as work orders that were issued by the base. We found that 27 of the 33 projects did not document a planned completion date or failed to meet the timelines they had established. Four other projects under \$1 million were managed centrally. All 4 were delivered later than planned. We could not obtain sufficient documentation on cost estimates to determine if projects that cost less than \$1 million were delivered within original cost estimates or if there was a relationship between any project cost overrun and the length of time it took to complete a project.

5.29 Departmental officials told us that owing to low expenditure approval thresholds and time delays, the processes escalate costs and sometimes result in projects not being delivered. This is particularly so for projects over \$1 million, since at any time in the project review process, the project may be held up with requests for information or new analysis.

5.30 In May 2009, National Defence tried to address this situation by streamlining the approval process for real property projects that were low risk. However, the Department reports that this effort did not ensure that projects consistently begin with minimal delay. A 2011 Army study of the approval process for real property projects costing over \$5 million counted numerous steps in the approval process before the project was ready to tender. The study calculated over six years to obtain approval. Thereafter, tendering and construction would be necessary before final delivery. A separate departmental study in 2011 also noted a long and bureaucratic approvals process that required over six years on average to obtain approvals and to complete a construction project. It also observed that in comparison, the private sector completes an equivalent project in an average of about three years.

5.31 Lengthy approval processes can delay the completion of a project and make it difficult to ensure that real property is in place at the right time. Department officials advised us that they have begun a complete review of the project delivery process in order to shorten project delivery times and that the Assistant Deputy Minister (Infrastructure and Environment) has begun to redesign delivery of the Department's construction program.

5.32 Recommendation. National Defence should simplify its approval processes for real property projects over \$1 million according to level of risk.

The Department's response. Agreed. In April 2012, National Defence initiated a comprehensive departmental review with the objective of reducing the project approval process time. As part of the National Defence Infrastructure and Environment Transformation Initiative and the Infrastructure and Environment Business Modernization program, all project approval, costing, and implementation procedures will be reviewed, redesigned, and documented.

5.33 Recommendation. National Defence should set and document firm timelines for the completion of real property projects under \$1 million and document cost estimates.

The Department's response. Agreed. As part of the National Defence Infrastructure and Environment Transformation Initiative and the Infrastructure and Environment Business Modernization program, all project implementation procedures and timelines will be reviewed, redesigned, and documented by April 2014.

National Defence has not fully implemented its financial controls over Defence Construction Canada

5.34 In 2008, National Defence and Defence Construction Canada signed a memorandum of understanding (MOU) that defines their relationship. We examined the financial and management control framework exercised by National Defence to ensure Defence Construction Canada carries out its obligations under the MOU and that projects are being executed by Defence Construction Canada according to the project plan and budget.

5.35 Under the MOU, National Defence has delegated to Defence Construction Canada the financial authority to authorize payment of third-party contracts. National Defence specified in the MOU that it will conduct cyclical reviews of relevant Defence Construction Canada financial management processes and perform semi-annual reviews of the Corporation's processes to verify requisitions and payments to contractors. These reviews should verify that delegated authorities are being exercised correctly and that Defence Construction Canada is ensuring requisitions and payments to contractors are properly made. We examined these key review controls to verify whether they were in place and operating at National Defence.

5.36 We found that the Department's key controls of cyclical and semi-annual reviews are not being fully implemented. Cyclical reviews have not been carried out since the signing of the 2008 MOU. National Defence has made some effort to conduct the semi-annual reviews, but these were limited to the national headquarters area and we found the methodology was flawed. Consequently, National Defence has not obtained assurance that delegated authorities are being exercised correctly by Defence Construction Canada to ensure requisitions and payments to contractors are properly made. National Defence has recognized that these controls are not operating effectively and, to the end of the audit, had not yet implemented corrective actions.

5.37 Project managers within National Defence also exercise a number of management controls to ensure Defence Construction Canada is properly managing construction, recapitalization, and maintenance and repair contracts. These controls may include activities such as ongoing budget monitoring and regular team meetings. They vary considerably depending on whether the project is valued at over \$1 million and managed centrally or valued at less than \$1 million and managed at the base level. We examined 11 projects valued at more than \$1 million and 4 projects valued at less than \$1 million in order to determine if

the control framework available to National Defence project managers was well designed and applied.

5.38 We found that for the projects valued at more than \$1 million, the management controls available to departmental project managers were adequate to monitor whether contracts managed by Defence Construction Canada were being executed according to the project plan and budget. In addition, we found that the project managers had properly applied the controls. For those projects valued at less than \$1 million, the management control framework available to departmental project managers is simplified but also adequate, and the controls were being properly applied.

5.39 Recommendation. National Defence should ensure that the cyclical and semi-annual review controls over Defence Construction Canada are implemented.

The Department's response. Agreed. National Defence will engage an independent third party to conduct semi-annual reviews of Defence Construction Canada's (DCC) processes for compliance with sections 33 and 34 of the *Financial Administration Act*. These reviews will commence in the 2012–13 fiscal year. Further, starting in the 2013–14 fiscal year, National Defence will incorporate consideration of cyclical reviews of the controls over DCC into its risk-based management processes.

The performance management framework for real property is incomplete

5.40 An effective performance management framework is based on an information system that collects relevant asset, financial, and program information and allows management to report on usage, maintenance, and overall performance of the Department's real property. Such a framework also provides the basis for managing risks. We examined whether there is a performance management framework and whether real property objectives and targets had been communicated to bases in a timely manner. In addition, we examined whether National Defence had monitored achievement of those objectives and targets.

5.41 We found that the performance measurement framework is incomplete and headquarters are unable to fully assess the state of the Department's real property assets. There is no central information system for performance management. However, some performance information is regularly collected at the national level, including measures of capital project completion and investment in maintenance and repair. The Assistant Deputy Minister (Infrastructure and

Environment) has also conducted two general surveys of selected aspects of infrastructure suitability and condition. Health and safety compliance is monitored through a variety of base and national processes. Nonetheless, bases have not received performance objectives and targets for important performance indicators, such as the condition or suitability of their real property.

5.42 National Defence has characterized performance measurement for real property at bases as developmental and inconsistent. We found some bases developed their own information management tools for monitoring performance (Exhibit 5.2).

Exhibit 5.2 Some bases have developed information management tools

The Navy bases at Esquimalt and Halifax have purchased commercial software to help manage their real property portfolios. The software is widely used in the private sector and systematically records information about individual buildings and works, and their internal systems, to provide a comprehensive assessment of each asset's condition. Managers use this information to cost and schedule infrastructure maintenance and repair investments several years in advance.

The Navy has found that the software enables it to make business decisions that are better informed than decisions made based on general assessments provided in the surveys conducted by the Assistant Deputy Minister (Infrastructure and Environment). The Department's research and development agency has reviewed the use of the commercial software and recommended full integration of the system into base engineering and construction organizations across the Department.

5.43 In 2009, the Assistant Deputy Minister (Infrastructure and Environment) started an Infrastructure and Environment Business Modernization program to develop Department-wide information management and accounting systems. The program will provide new information capabilities for base-level inspection and maintenance management, timely performance management, and portfolio management. By the end of the audit period, the business modernization program had begun to coordinate planning with the Navy information management initiative. The planned date of implementation, including data collection, has been changed from March 2014 to April 2015.

5.44 Recommendation. National Defence should implement a performance management framework that sets performance targets such as for condition, suitability, and safety of its real property.

The Department's response. Agreed. National Defence will enhance its performance management framework to support real property decision making at all levels. Performance management will be

supported through a national enterprise resource planning information system that will facilitate all real property performance management by March 2014.

5.45 Recommendation. National Defence should ensure that initiatives and lessons learned at the bases are incorporated into the development of its new management information system under the Infrastructure and Environment Business Modernization program.

The Department's response. Agreed. As part of the Infrastructure and Environment Business Modernization Program, 35 workshops have been conducted to draw on base-level expertise. Input and participation will continue to be sought from representatives across the Royal Canadian Navy, Canadian Army, and the Royal Canadian Air Force to ensure that lessons learned are incorporated.

Preventive maintenance practices are insufficient

5.46 Preventive maintenance is an essential maintenance and repair practice for appropriate life-cycle management and risk management. Preventive maintenance is needed to optimize the useful life of real property and appropriately mitigate health and safety risks. We examined whether the Department implemented preventive maintenance practices.

5.47 In our survey of 21 main bases across Canada, several bases reported that their preventive maintenance programs stopped during the mid-1990s because of personnel and financial cutbacks. The Assistant Deputy Minister (Infrastructure and Environment) has reported that stopping the preventive maintenance programs over the last decade has directly contributed to premature building and internal systems failures. The Department reports that bases have been using available maintenance and repair funding to perform immediately required corrective actions instead of spending funds on preventive measures to reduce the need for future immediate corrective maintenance. The result is that a base's real property portfolio continuously deteriorates.

5.48 Through our survey, we asked bases whether preventive maintenance was being conducted. Eleven of 21 bases reported some level of preventive maintenance. Two of these 11 reported that full preventive maintenance has been contracted out and is being done. Ten bases reported not having a preventive maintenance program. Four bases stated they focus on maintenance after breakdowns rather than focusing on preventive maintenance.

5.49 Starting in the 2011–12 fiscal year, the Assistant Deputy Minister (Infrastructure and Environment) directed custodians to establish a program of preventive maintenance tasks that meet legislative requirements and that, if not performed, may lead to immediate loss of facility functions or to safety hazards. Custodians were told to incrementally expand this first step until they establish an ongoing full preventive maintenance program by the 2014–15 fiscal year. During the audit, the Assistant Deputy Minister (Infrastructure and Environment) also began to establish a national program to identify minimum maintenance tasks that must be performed and recommend strategies for completing those tasks.

National Defence has reported some non-compliance with health and safety policies

5.50 The condition of real property can impact health and safety. We examined whether the Department ensures that its infrastructure does not pose a risk to health and safety. Real property managers must track conditions very closely and be sure that funds are planned and invested to maintain condition, make improvements, and deal with risks as they arise (see Exhibit 5.3).

Exhibit 5.3 The planned late delivery of a project has created health and safety risks

Lord Strathcona's Horse (Royal Canadians) is an armoured regiment that has tanks and is located at Canadian Forces Base Edmonton. In March 2012, the regiment received delivery of the first of 44 new main battle tanks and armoured recovery tanks. The vehicles were acquired as part of a program that began in 2007 in response to an urgent operational requirement for new tanks to support troops in Afghanistan. There was not enough money to upgrade all necessary infrastructure at that time. Planning for the construction of needed buildings at Canadian Forces Base Edmonton and another base did not begin until 2009. National Defence has stated that no new infrastructure to house the new tanks will be provided at the base before 2016.

While awaiting the design, approval, and construction of a new facility, the regiment must maintain its tanks in a building that was originally designed as a garage for vehicle storage. Until the existing exhaust and ventilation system is properly fixed or replaced, personnel must operate with bay doors open to ventilate, which is only practical during temperate months. According to a Canadian Forces medical assessment, noise levels may be causing permanent hearing damage to the workers. Personnel also lack barrier protection between themselves and the engines while the engines are being tested. Should there be a catastrophic failure of engine components, projectiles and hot engine fluids could pose a serious hazard to nearby workers.

As a risk-management solution, personnel are required to use recommended ear defenders over ear plugs while working in the immediate area and an alarm was installed to warn personnel to wear the prescribed hearing protection. During the audit, the base installed an exhaust fan to improve air quality in the meantime.

5.51 Under the *Canada Labour Code*, Part II, National Defence has a duty to ensure the health and safety of all of its civilian workers. The Canadian Forces is not part of the public service, and its military members are not covered by the *Canada Labour Code*. However, National Defence policy commits it to ensuring that a similar level of safety precautions for its military personnel is incorporated into all aspects of its operations, training, and support activities. Although accomplishing missions is the top priority, commanding officers are to consider safety in every aspect of military operations to ensure that their people are not put at needless risk and material resources are not needlessly depleted by accidents.

5.52 Responsibility for health and safety is shared among the Assistant Deputy Minister (Infrastructure and Environment), the Vice Chief of the Defence Staff, and custodians. The Assistant Deputy Minister (Infrastructure and Environment) and Vice Chief of the Defence Staff provide centralized development of policies for health and safety in order to ensure consistency across all bases and to monitor compliance. Funding and accountability for compliance with health and safety policies rests with custodians; they in turn rely on base commanders to use local systems to identify risks to health and safety and to track compliance.

5.53 In our survey of all the 21 main bases, we asked how they deal with health and safety issues related to infrastructure. We also met with managers at headquarters and examined reports of compliance monitoring programs for fire safety, nuclear safety, radon testing, and architecture and engineering components, such as electrical, mechanical, water, and fuel storage systems.

5.54 We found that all bases we surveyed reported that they have active programs to identify and report on health and safety issues. Three of these bases reported that a lack of human or financial resources reduced their ability to fully address all identified issues.

5.55 Fire safety. The Canadian Forces Fire Marshal establishes policies and standards for fire protection and emergency fire operations, and reports to the Assistant Deputy Minister (Infrastructure and Environment) on bases' compliance with the National Fire Code of Canada and departmental policies. The Fire Marshal also reports instances of non-compliance with the *Canada Labour Code*, Part II; the Treasury Board Fire Protection Standard; and National Defence policy to custodians and base commanders through a national cyclical compliance review. Custodians and base commanders are responsible for correcting reported shortcomings.

5.56 The Fire Marshal tracked 278 fires to non-residential real property in the three-year period between 1 January 2008 and 31 December 2010. During this period, fire destroyed most of the Grande-Allée Armoury in Quebec City, one of Canada's most historic armouries. Of the \$31 million of damages and losses to non-residential property that were caused by the 278 fires, the Armoury loss was estimated at \$25 million. A key finding in the Fire Marshal's investigation of the fire was that the fire alarm system had been partially disabled, which caused a delay in detecting the fire and contributed to the loss. Furthermore, it was determined that the system had not been maintained, inspected, and tested as required by the National Fire Code of Canada. In addition, the Fire Marshal's ongoing compliance review identified a widespread lack of departmental compliance with the National Fire Code of Canada with respect to the inspection, testing, and maintenance of fire protection systems. Based on the armoury fire investigation and the ongoing compliance review, the Deputy Minister and Chief of the Defence Staff issued a joint letter in January 2009 ordering custodians to address the deficiencies raised by the Canadian Forces Fire Marshal and to make monthly reports to the Assistant Deputy Minister (Infrastructure and Environment).

5.57 The Canadian Forces Fire Marshal fire protection program review verifies that fire inspection and protection programs are in compliance with fire codes and regulations at selected locations across Canada. For the period from January 2008 to June 2011, the Canadian Forces Fire Marshal conducted a review of compliance with various aspects of the Department's fire protection program at 45 locations. Twenty-eight of 45 reviewed locations received a less than satisfactory rating for overall compliance. The compliance review of fire alarms inspection, testing, and maintenance recorded that 31 percent of reviewed locations were not conducting monthly inspections of fire alarms in accordance with the National Fire Code of Canada, while 18 percent were deficient in performing required annual inspections.

5.58 Twenty of these 28 locations did not produce corrective action plans within 90 days of the Fire Marshal's report as required. We were unable to determine if another 3 of the 28 locations that received less than a satisfactory rating for overall compliance had produced the required plans in a timely manner. Five of the 28 locations that received less than a satisfactory rating for overall compliance still had not produced an action plan by the end of our audit period.

5.59 We noted that the Canadian Forces Fire Marshal oversees compliance with the Department's fire protection program by base commanders and reports findings to the custodians but does not have

the authority to compel base commanders to act on his findings. Owing to the serious nature of our findings in this area, we sent a letter to the Deputy Minister and Chief of the Defence Staff outlining our concerns about the reported instances of non-compliance with the National Fire Code of Canada. The Department has acknowledged that compliance with the National Fire Code of Canada is essential and is taking action to implement a program to bring all bases into full compliance.

5.60 Other health and safety compliance programs. Evaluations by the Assistant Deputy Minister (Infrastructure and Environment) found low compliance with requirements related to intrusion alarm and detection systems. Evaluations also found that five locations were not satisfactorily compliant with procedures to monitor indoor air quality.

5.61 There are also monitoring programs for nuclear safety and radon testing. National Defence uses x-ray devices for security screening and non-destructive testing of its equipment. The nuclear safety compliance program monitors operation, storage, and disposal of these and other nuclear devices. We found bases had produced action plans when the monitoring program for nuclear safety observed deficiencies. The radon program does not require action plans to be produced.

5.62 In summary. National Defence is not meeting important legislative, regulatory, and policy requirements related to health and safety within its real property portfolio. This could put the health and safety of workers in the affected facilities at risk.

5.63 Recommendation. National Defence senior management should take quick action to fully remedy all situations of non-compliance with applicable health and safety legislation, regulations, and policies.

The Department's response. Agreed. National Defence has taken and will continue to take action to remedy situations of non-compliance, including:

- implementing a national solution to provide bases with additional capacity to execute inspection, testing, and maintenance of fire protection systems; and
- implementing an architecture and engineering assistance and compliance program to ensure that buildings and systems comply with national codes, standards, laws, and, where applicable, provincial ones.

Resource management

5.64 We examined National Defence's achievement against the *Canada First Defence Strategy* targets and departmental targets for infrastructure spending, which is how the Department measures and reports on its real property performance. We also examined whether National Defence, under its current management processes, has the workforce it requires to support its real property needs.

National Defence has not yet reached its expenditure targets for maintenance and repair and recapitalization

5.65 National Defence's expenditure targets for maintenance and repair and recapitalization are based on the cost to replace its aging infrastructure, known as the realty replacement cost. We analyzed the accuracy of the Department's realty replacement cost through our sample of 49 projects completed during the audit period. We obtained detailed spending data on maintenance and repair and on capital spending from the 21 main bases that we surveyed, and compared the information with departmental targets. We also confirmed base data with each of the Army, Air Force, Navy, and Chief Military Personnel commands and the departmental accounting system. We completed our analysis with information from the Assistant Deputy Minister (Infrastructure and Environment) in order to obtain the departmental perspective.

5.66 Canada First Defence Strategy commitment. The *Canada First Defence Strategy* targets 8 percent (\$40 billion of \$490 billion) of the total departmental budget over 20 years up to the 2027–28 fiscal year to be spent on real property. We found that for the 2010–11 fiscal year, National Defence spent about 3 percent of its \$22.8 billion budget on real property. This means that the Department will have to spend at a greater rate in coming years if it is going to meet the overall real property commitment in the *Canada First Defence Strategy*.

5.67 Realty replacement cost. At the beginning of the 2010–11 fiscal year, the Department calculated its total realty replacement cost at \$21.7 billion. Industry standards and Treasury Board guidelines recommend a minimum annual investment of 4 percent of realty replacement cost to maintain, repair, and recapitalize real property. The *Canada First Defence Strategy* target for recapitalization and maintenance and repair of National Defence real property is just under 4 percent of realty replacement cost per year. The Department has set its own targets to be 2.5 percent for recapitalization and 2 percent for maintenance and repair. The 2 percent of realty replacement cost target for maintenance and repair has been further broken down to 1.4 percent for direct expenditures and 0.6 percent for salaries and wages.

5.68 Correct calculation of realty replacement cost depends on accurate data and valuation of realty assets. A 2009 review conducted by the Department of the methodology it uses to calculate its realty replacement cost found the calculation could under- or overestimate realty replacement costs by up to 20 percent. Our examination of 49 new construction projects found that for the buildings and works completed in the audit period, the Department's realty asset information system had understated the total realty replacement cost of the projects by at least 45 percent compared with the recorded acquisition costs (known as historical costs) from its financial system. For example, one recently constructed truck shelter, recorded in the financial system at \$893,000 historical cost, had a recorded realty replacement cost of \$395,000. In another case, a new control tower constructed at Canadian Forces Base Trenton with a historical cost of \$14.6 million had a recorded realty replacement cost of \$5.2 million.

5.69 Despite the risk that realty replacement cost may be understated, National Defence sets its expenditure targets and allocates its budgets for infrastructure maintenance and repair and recapitalization based on its calculation of realty replacement cost. This means that investments based on realty replacement cost may not be enough to maintain and repair or recapitalize the Department's real property.

5.70 **Spending on maintenance and repair.** The Department reports that it spent about \$189 million on maintenance and repair, not including salaries and wages, during the 2010–11 fiscal year. This amounts to about 0.9 percent of realty replacement cost, substantially less than its own target of 1.4 percent. National Defence revised the target to 1.2 percent and 1.4 percent for the 2012–13 and 2013–14 fiscal years, respectively. Officials informed us that departmental expenditures for maintenance and repair increased to 1.0 percent of realty replacement cost in the 2011–12 fiscal year.

5.71 We obtained maintenance and repair expenditures for the 2010–11 fiscal year for 19 of the 21 main bases across Canada that we surveyed. We note that this was the first year that maintenance and repairs had been accounted for as a separate expenditure item, allowing these 19 bases to know their performance against the target. The maintenance and repair at 2 of the 21 main bases is funded through contract agreements that do not enable annual costs of maintenance and repair to be identified.

5.72 We found that 10 of the 19 main bases across Canada that identified maintenance and repair expenditures spent less than 0.7 percent of realty replacement cost on maintenance and repair,

or half of the departmental target. Only 1 base spent enough to achieve the 1.4 percent target for maintenance and repair in the 2010–11 fiscal year (Exhibit 5.4).

5.73 National Defence has not yet met its targets for spending on maintenance and repair. Infrastructure is likely to continue deteriorating until the Department consistently meets the minimum standard level of spending according to *Canada First Defence Strategy* targets and Treasury Board guidelines.

Exhibit 5.4 Only one main base met the Department's spending target for maintenance and repair in the 2010–11 fiscal year



*5 GSS: Refers to 5 Area Support Group that combines the bases at Montréal, Valcartier, and St-Jean.

Source: National Defence financial system

5.74 Recapitalization. Consistent with the *Canada First Defence Strategy* and Treasury Board targets, the Department has committed to a yearly recapitalization rate of 2.5 percent of realty replacement cost. The strategy clearly differentiates investments in recapitalization from investments for new infrastructure. Currently, the Department's accounting systems do not distinguish between recapitalization and capital expenditures for new real property. National Defence includes in its reporting against the recapitalization target of 2.5 percent all spending for recapitalization as well as for new real property. This means its reporting overstates the percentage spent on recapitalization.

5.75 The 2010–11 Departmental Performance Report stated that National Defence had achieved its annual recapitalization expenditure target of 2.5 percent of realty replacement cost. However, the \$509 million amount for recapitalization reported as spent of a planned \$710 million included unspecified amounts for new buildings and works, as well as some costs for items such as furniture that are not real property and associated immovable assets. As these expenditures should not have been included in the reported amount, the Department did not meet the target for spending on recapitalization.

5.76 In summary. Unless the Department is able to increase expenditures to meet its targets for maintenance and repair and recapitalization of real property, it will not meet the *Canada First Defence Strategy* or Treasury Board policy guidelines for life-cycle management investment and will continue to fall behind in renewal of its real property.

5.77 Recommendation. National Defence should ensure its calculation of realty replacement cost is accurate.

The Department's response. Agreed. National Defence follows common industry methodology for calculation of realty replacement cost as a proxy measure of portfolio value for purposes of maintenance and repair allocation. National Defence will improve the accuracy of the calculation of the realty replacement cost for the National Defence portfolio as part of the Infrastructure and Environment Business Modernization program by the end of the 2013–14 fiscal year.

5.78 Recommendation. National Defence should change its accounting systems so that it can clearly separate expenditures on recapitalization and construction of new buildings and works.

The Department's response. Agreed. National Defence will change its accounting system in order to better define real property expenditures and clearly separate expenditures for new construction versus recapitalization. The Department Resource Management Information System (DRMIS) will be modified to differentiate expenditures for real property recapitalization and for the construction of new buildings effective 1 April 2013. This will be incorporated into capital construction program management and the process for the Capital Investment Plan (Infrastructure) (2013–2023).

5.79 Recommendation. National Defence should develop a strategy that will enable it to reach its *Canada First Defence Strategy* targets for maintenance and repair and recapitalization.

The Department's response. Agreed. The National Defence Real Property Strategy will provide the vision and direction to support the *Canada First Defence Strategy* intention with respect to infrastructure.

Bases do not receive timely funding to meet their real property requirements

5.80 We examined whether bases received sufficient funding in a timely manner in order to reach real property investment goals. We found that bases often did not begin to receive funding for maintenance and repair projects and for capital projects of less than \$1 million until well into the first quarter of the fiscal year. In four instances, this funding was not received until the second quarter and in another four cases, not until the third quarter.

5.81 Custodians allocated additional amounts throughout the year, so while bases knew their notional allocation ahead of time, they did not know with certainty their actual available funds for the year or when they would receive those funds. Through the 2010–11 fiscal year, the 19 main bases for which we obtained maintenance and repair expenditures received a total additional 66 percent over their initial allocation in funding for capital spending. Forty-one percent of these additional capital funds were received in the third and fourth quarters of the fiscal year. In the same fiscal year, for maintenance and repair, the 19 main bases were allocated 59 percent in additional funding over their initial allocation. Two thirds of this additional funding for maintenance and repair was received in the third and fourth quarters of the 2010–11 fiscal year.

5.82 Officials at bases told us that the late arrival of funds creates a challenge as the receipt of funds and the ability to commit funds do not match construction cycles. In the construction business, calls for tender are usually issued over the winter, contracts are awarded in the spring, and work begins in spring or early summer. Without clear advance approval of real property budgets, bases are at risk of not being able to align project planning and execution with the construction cycle.

5.83 The Department stated that it will centralize management of its annual funds for construction into a single account starting in the 2012–13 fiscal year. Approximately half of the funds would be invested in construction projects costing more than \$5 million and be managed by the Assistant Deputy Minister (Infrastructure and

Environment) so any necessary adjustments can be addressed nationally. The other half of the funds would be available for projects that cost less than \$5 million and have low risk. Custodians are to manage these projects in a way that is consistent with corporate priorities but responsive to local priorities.

5.84 The Assistant Deputy Minister (Infrastructure and Environment) has advised custodians that when planning construction projects over \$1 million, they may over plan by approximately 60 percent to compensate for delays and non-performance of construction projects. Overplanning is when custodians have committed, spent, and planned to execute additional activities for which funding was not initially available but funding is anticipated due to expected project delays and stoppages.

5.85 Recommendation. National Defence should approve and allocate funding to bases in time to plan and execute projects consistent with the construction cycle.

The Department's response. Agreed. National Defence will set target distribution dates and monitor release of funds on an annual basis commencing in April 2013. Custodians will be directed to provide annual and three-year forecast resource allocations to bases and wings for the 2013–14 fiscal year.

With respect to capital projects, the 2012–13 fiscal year is the first year of a consolidated capital program, which resulted in timely distribution of funds to approved and planned projects.

Fundamental change is required in the way National Defence manages its resources to support real property

5.86 The *Canada First* Defence Strategy requires a balance of investments in personnel with financial investments in infrastructure. The Department must find ways to meet the strategy commitments for renewing its infrastructure while at the same time implementing government cutbacks.

5.87 The Department reports that shortages of skilled and qualified real property personnel are being felt at all levels, from the base construction engineering organization to headquarters support organizations. National Defence reports that since budget cuts in the 1990s, its real property workforce has been insufficient. Since 2010, the government has ordered a number of government-wide cost-cutting initiatives that have had a direct impact on numbers of employees allowed for the Department.

5.88 We examined whether the Department has ensured bases have the human resources they need to deliver the real property program under its current methods of operation. Our survey asked for information on human resource needs and we examined the organization charts for real property functions provided to us by base commanders. We also inquired at headquarters about the departmental implementation of government-wide reductions in personnel announced in recent federal budgets.

5.89 Nineteen of the 21 main bases reported they had positions not filled. We found that 9 of 21 bases surveyed reported a rate of 15 percent or greater of civilian positions that were not filled. And 7 of 21 bases surveyed reported a rate of 15 percent or greater of military positions that were not filled. Each year, base commanders estimate requirements for civilian staff and submit these through the chain of command to custodians, where they are prioritized against available resources that have been allocated through the Department's business planning process. Bases are provided with a salary and wage budget envelope and are required to manage within that envelope.

5.90 Bases and the Department as a whole report that human resource shortages prevent comprehensive life-cycle management and limit their ability to carry out real property projects. This results in real property work often not being done in a timely and coordinated manner, with associated risks to the quality of work. National Defence has stated that military and civilian real property staffs are stretched thin, with risks of undue stress and burnout, and that junior staff have been taking on responsibilities beyond their capacities.

5.91 Under the current way of doing business, base requirements for civilian employees significantly exceed available human resources. In 2011, custodians estimated additional necessary staffing requirements of 579 real property positions. The Department approved funds for 16.5 of these positions.

5.92 National Defence cannot expect a significant increase in its real property workforce. In the 2012 Budget, the government announced plans to reduce defence expenditures. Reductions will be achieved in part through civilian workforce downsizing while the number of Canadian Forces members will be maintained. Human resource gaps could also be filled by contractors, but the Department also plans to reduce its reliance on professional services contractors.

5.93 Consequently, in our opinion, the Department will not be able to continue to manage its real property using the processes currently in place. It does not have, and will not have, the human resources to do so.

5.94 During the audit period, the Assistant Deputy Minister (Infrastructure and Environment) began planning an initiative to transform delivery of real property services. The planned initiative will analyze the current state of the Department's real property portfolio; the overall status of human resources; and the existing buildings, lands, works and equipment available to base construction and engineering organizations. An analysis will include study of best practices in other government, private sector and foreign military organizations. However, the Assistant Deputy Minister (Infrastructure and Environment) has noted that, due to current human resource limitations, focus on this initiative may postpone completion and publication of the Real Property Management Framework, writing and publication of a performance management strategy, and implementation of a national preventive maintenance program.

5.95 Recommendation. National Defence senior management should complete the transformation of its real property business model that should include an integrated real property financial and human resource strategy.

The Department's response. Agreed. Budget 2012 announced that National Defence will centralize real property management. National Defence has launched an Infrastructure and Environment Transformation Initiative to achieve this objective.

Conclusion

5.96 National Defence acknowledges that it needs to transform the way in which it manages its real property. It has started to put in place some of the components required to do so and is planning to do more. While we found that National Defence has exercised some requirements of sound stewardship, we determined that the Department has not yet exercised all the elements of sound stewardship required to manage its real property. It has important areas for improvement in planning; management practices for acquiring, recapitalizing, maintaining, and repairing capital assets; performance management; compliance with health and safety policies; and management of financial and human resources.

5.97 National Defence is falling behind in meeting the targets set out in the *Canada First Defence Strategy* for real property infrastructure investment. As such, the weaknesses noted in National Defence's management of real property can jeopardize the Canadian Forces' ability to carry out the missions stated in the strategy.

About the Audit

All of the audit work in this chapter was conducted in accordance with the standards for assurance engagements set by The Canadian Institute of Chartered Accountants. While the Office adopts these standards as the minimum requirement for our audits, we also draw upon the standards and practices of other disciplines.

Objectives

The audit objective was to determine whether National Defence has exercised sound stewardship in managing its real property.

The audit was divided into three sub-objectives:

- To determine whether National Defence has exercised sound stewardship in clearly defining, budgeting for, and communicating to bases present and future real property needed to generate (organize, train, equip) and project (rapidly deploy) forces.
- To determine whether National Defence has exercised sound stewardship in providing new infrastructure and recapitalization to bases in response to operational requirements for force generation and projection.
- To determine whether National Defence has identified and provided the human resources it needs to acquire and sustain infrastructure at bases.

Scope and approach

The audit focused on operations and expenditures during the 2010–11 fiscal year and the first two quarters (1 April to 30 September) of the 2011–12 fiscal year. We also examined National Defence's oversight of contract work performed by Defence Construction Canada.

We interviewed National Defence officials, Canadian Forces members, and civilian employees of National Defence located in National Defence's headquarters in Ottawa and at Canadian Forces bases across Canada. We visited Army bases in Edmonton, Wainwright, Suffield, and Montréal; Air Force wings in Winnipeg, Cold Lake, Greenwood, and Shearwater; and Navy bases in Esquimalt and Halifax, including the ammunition depot in Bedford.

The audit administered a survey to the base commanders of 21 bases that were identified by the Army, Air Force, Navy, and Chief Military Personnel as the main bases responsible for force generation and force projection. The survey was directed to base commanders and asked questions about construction engineering, operations, project management, personnel management, and health and safety over the period of the audit. The base commanders replied to this survey and provided necessary documentation to support their replies. We then followed up as necessary with higher levels of command and headquarters. Survey responses were examined and verified through review of related documents and data from central information systems.

We chose a sample of infrastructure capital projects from National Defence's realty asset accrual accounting system that were completed during the time period of the audit. The sample was taken from a total data population of 172 projects and consisted of 41 capital projects that were completed during the audit period and were valued at less than \$5 million each. We also examined all 8 capital projects valued in excess of \$5 million that were completed during the audit period, for a total of 49 projects examined.

Criteria

| Criteria | Sources |
|---|---|
| To determine whether National Defence has exercised sound stewardship in clearly defining, budgeting for, and communicating to bases present and future real property needed to generate and project forces, we used the following criteria: | |
| National Defence has clearly defined present and future real property needs to generate and project forces. (Sources: 2, 3, 4) | 1. Canada Labour Code 2. Policy on Management of Real Property, Treasury Board 3. Policy on Financial Management Governance, Treasury Board 4. Policy Framework for the Management of Assets and Acquired Services, Treasury Board 5. Policy on Financial Resource Management, Information and Reporting, Treasury Board 6. Occupational Safety and Health, Treasury Board, 1994 7. Fire Protection Standard, Treasury Board of Canada Secretariat 8. Defence Administrative Order and Directive 4001–0, Management of Realty Assets, National Defence, 2002 9. Defence Administrative Order and Directive 4001–1, Realty Asset Life Cycle Management, National Defence, 2002 10. Defence Administrative Order and Directive 2007–0, Safety, 2004 11. Defence Administrative Order and Directive 2007–1, General Safety Program, 2002 |
| National Defence communicates its real property plans to wings and bases in a timely manner. (Sources: 2, 8) | |
| National Defence is monitoring requirements to maintain real property for operations. (Sources: 2, 8) | |
| Bases have the financial resources that National Defence has identified are needed to sustain base real property for operations. (Sources: 5, 9) | |
| National Defence ensures infrastructure does not present hazards or risks to the health or safety of personnel. (Sources: 1, 6, 7, 10, 11) | |
| To determine whether National Defence has exercised sound stewardship in providing new infrastructure and recapitalization to bases in response to operational requirements for force generation and projection, we used the following criteria: | |
| Delivery of major new real property infrastructure and recapitalization at bases is aligned with planned timelines and full costs. (Sources: 12, 13, 17) | 12. Policy on Management of Real Property, Treasury Board 13. Policy Framework for the Management of Assets and Acquired Services, Treasury Board 14. Contracting Policy, Treasury Board 15. Policy on the Management of Projects, Treasury Board, 2009 16. Framework for the Management of Risk, Treasury Board of Canada Secretariat |
| National Defence ensures that major new infrastructure and recapitalization constructed at bases satisfy identified requirements. (Sources: 13, 14, 15) | |

| Criteria | Sources |
|---|---|
| <p>To determine whether National Defence has exercised sound stewardship in providing new infrastructure and recapitalization to bases in response to operational requirements for force generation and projection, we used the following criteria: (continued)</p> | |
| <p>National Defence has implemented the financial management and management control systems to measure the effective delivery of its infrastructure projects.</p> <p>(Sources: 13, 15, 18)</p> | <p>17. Project Approval Guide, National Defence, 2009</p> <p>18. Memorandum of Understanding between National Defence and Defence Construction Canada (1951) Limited, 2008</p> |
| <p>National Defence has implemented an effective risk management process to manage its infrastructure projects delivered by Defence Construction Canada.</p> <p>(Sources: 15, 16)</p> | |
| <p>To determine whether National Defence has identified and provided the human resources it needs to acquire and sustain infrastructure at bases, we used the following criteria:</p> | |
| <p>National Defence ensures bases have the human resources they need to maintain real property and provide major new infrastructure and recapitalization.</p> <p>(Sources: 19, 20)</p> | <p>19. Policy Framework for People Management, Treasury Board</p> <p>20. Recommended General Criteria and Sub-Criteria for Human Resource Management, Office of the Auditor General of Canada, 2010</p> |

Management reviewed and accepted the suitability of the criteria used in the audit.

Period covered by the audit

The audit covered the period 1 April 2010 to 31 December 2011. Audit work for this chapter was completed on 17 July 2012.

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Appendix List of recommendations

The following is a list of recommendations found in Chapter 5. The number in front of the recommendation indicates the paragraph where it appears in the chapter. The numbers in parentheses indicate the paragraphs where the topic is discussed.

| Recommendation | Response |
|--|--|
| Planning for real property needs | |
| <p>5.19 National Defence should complete development of and implement its Real Property Strategy, Real Property Management Framework, and national master real property development plan. (5.13–5.18)</p> | <p>Agreed. National Defence, through the Infrastructure and Environment Transformation Initiative, is taking all necessary actions to complete the development and implementation of its Real Property Strategy and Real Property Management Framework. The development of the National Real Property Development Plan is under way and will be coordinated with the Department's investment planning cycle.</p> |
| Real property management practices | |
| <p>5.32 National Defence should simplify its approval processes for real property projects over \$1 million according to level of risk. (5.21–5.31)</p> | <p>Agreed. In April 2012, National Defence initiated a comprehensive departmental review with the objective of reducing the project approval process time. As part of the National Defence Infrastructure and Environment Transformation Initiative and the Infrastructure and Environment Business Modernization program, all project approval, costing, and implementation procedures will be reviewed, redesigned, and documented.</p> |
| <p>5.33 National Defence should set and document firm timelines for the completion of real property projects under \$1 million and document cost estimates. (5.21–5.31)</p> | <p>Agreed. As part of the National Defence Infrastructure and Environment Transformation Initiative and the Infrastructure and Environment Business Modernization program, all project implementation procedures and timelines will be reviewed, redesigned, and documented by April 2014.</p> |
| <p>5.39 National Defence should ensure that the cyclical and semi-annual review controls over Defence Construction Canada are implemented. (5.34–5.38)</p> | <p>Agreed. National Defence will engage an independent third party to conduct semi-annual reviews of Defence Construction Canada's (DCC) processes for compliance with sections 33 and 34 of the <i>Financial Administration Act</i>. These reviews will commence in the 2012–13 fiscal year. Further, starting in the 2013–14 fiscal year, National Defence will incorporate consideration of cyclical reviews of the controls over DCC into its risk-based management processes.</p> |

| Recommendation | Response |
|---|--|
| <p>5.44 National Defence should implement a performance management framework that sets performance targets such as for condition, suitability, and safety of its real property. (5.40–5.43)</p> | <p>Agreed. National Defence will enhance its performance management framework to support real property decision making at all levels. Performance management will be supported through a national enterprise resource planning information system that will facilitate all real property performance management by March 2014.</p> |
| <p>5.45 National Defence should ensure that initiatives and lessons learned at the bases are incorporated into the development of its new management information system under the Infrastructure and Environment Business Modernization program. (5.40–5.43)</p> | <p>Agreed. As part of the Infrastructure and Environment Business Modernization Program, 35 workshops have been conducted to draw on base-level expertise. Input and participation will continue to be sought from representatives across the Royal Canadian Navy, Canadian Army, and the Royal Canadian Air Force to ensure that lessons learned are incorporated.</p> |
| <p>5.63 National Defence senior management should take quick action to fully remedy all situations of non-compliance with applicable health and safety legislation, regulations, and policies. (5.50–5.62)</p> | <p>Agreed. National Defence has taken and will continue to take action to remedy situations of non-compliance, including:</p> <ul style="list-style-type: none"> • implementing a national solution to provide bases with additional capacity to execute inspection, testing, and maintenance of fire protection systems; and • implementing an architecture and engineering assistance and compliance program to ensure that buildings and systems comply with national codes, standards, laws, and, where applicable, provincial ones. |

Resource management

5.77 National Defence should ensure its calculation of realty replacement cost is accurate. (5.65–5.76)

Agreed. National Defence follows common industry methodology for calculation of realty replacement cost as a proxy measure of portfolio value for purposes of maintenance and repair allocation. National Defence will improve the accuracy of the calculation of the realty replacement cost for the National Defence portfolio as part of the Infrastructure and Environment Business Modernization program by the end of the 2013–14 fiscal year.

Recommendation**Response**

5.78 National Defence should change its accounting systems so that it can clearly separate expenditures on recapitalization and construction of new buildings and works. (5.65–5.76)

Agreed. National Defence will change its accounting system in order to better define real property expenditures and clearly separate expenditures for new construction versus recapitalization. The Department Resource Management Information System (DRMIS) will be modified to differentiate expenditures for real property recapitalization and for the construction of new buildings effective 1 April 2013. This will be incorporated into capital construction program management and the process for the Capital Investment Plan (Infrastructure) (2013–2023).

5.79 National Defence should develop a strategy that will enable it to reach its *Canada First* Defence Strategy targets for maintenance and repair and recapitalization. (5.65–5.76)

Agreed. The National Defence Real Property Strategy will provide the vision and direction to support the *Canada First* Defence Strategy intention with respect to infrastructure.

5.85 National Defence should approve and allocate funding to bases in time to plan and execute projects consistent with the construction cycle. (5.80–5.84)

Agreed. National Defence will set target distribution dates and monitor release of funds on an annual basis commencing in April 2013. Custodians will be directed to provide annual and three-year forecast resource allocations to bases and wings for the 2013–14 fiscal year.

With respect to capital projects, the 2012–13 fiscal year is the first year of a consolidated capital program, which resulted in timely distribution of funds to approved and planned projects.

5.95 National Defence senior management should complete transformation of its real property business model that should include an integrated real property financial and human resource strategy. (5.86–5.94)

Agreed. Budget 2012 announced that National Defence will centralize real property management. National Defence has launched an Infrastructure and Environment Transformation Initiative to achieve this objective.

Report of the Auditor General of Canada to the House of Commons

Matters of Special Importance

Main Points—Chapters 1 to 7

Appendices

Planning the Use of Professional Service Contractors

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CHAPTER 1

Transfer Payments to the Aerospace Sector—Industry Canada



Office of the Auditor General of Canada



Report of the Auditor General of Canada to the House of Commons

CHAPTER 6

Transfer Payments to the Aerospace Sector—Industry Canada



Office of the Auditor General of Canada

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CHAPTER 6

Transfer Payments to the Aerospace Sector— Industry Canada



Performance audit reports

This report presents the results of a performance audit conducted by the Office of the Auditor General of Canada under the authority of the *Auditor General Act*.

A performance audit is an independent, objective, and systematic assessment of how well government is managing its activities, responsibilities, and resources. Audit topics are selected based on their significance. While the Office may comment on policy implementation in a performance audit, it does not comment on the merits of a policy.

Performance audits are planned, performed, and reported in accordance with professional auditing standards and Office policies. They are conducted by qualified auditors who

- establish audit objectives and criteria for the assessment of performance;
- gather the evidence necessary to assess performance against the criteria;
- report both positive and negative findings;
- conclude against the established audit objectives; and
- make recommendations for improvement when there are significant differences between criteria and assessed performance.

Performance audits contribute to a public service that is ethical and effective and a government that is accountable to Parliament and Canadians.

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Transfer Payments to the Aerospace Sector—Industry Canada

Main Points

What we examined

Since 2007, Industry Canada has authorized assistance of almost \$1.2 billion through two transfer payment programs to the aerospace sector: the Strategic Aerospace and Defence Initiative (SADI) and the Bombardier CSeries Program. SADI is the federal government's second largest program of direct spending on research and development, created to support private sector industrial research and pre-competitive development in Canada's aerospace, defence, security, and space industries through repayable project contributions. The Department has 25 individual SADI projects with recipients.

Industry Canada also manages two repayable contribution agreements for the Bombardier CSeries Program. These contributions are intended to encourage research and development that will result in the development of new commercial aircraft technologies.

We examined whether Industry Canada had sufficient information to determine if the transfer payments were meeting the programs' objectives. We also looked at whether the Department managed these programs according to the key requirements of the Treasury Board's Policy on Transfer Payments and the terms and conditions of the programs. In addition, we examined whether Industry Canada collected repayments from recipients for contributions that are repayable under two previous transfer payment programs: the Defence Industry Productivity Program and Technology Partnerships Canada.

Audit work for this chapter was completed on 17 July 2012. More details on the conduct of the audit are in **About the Audit** at the end of this chapter.

Why it's important

The federal government regards the aerospace sector as crucial to Canada's economic development, sovereignty, national security, and public safety. Aerospace companies are important contributors to the Canadian economy. National Research Council Canada reported that Canada's aerospace sector is the fifth largest in the world, as of 2008, with total aerospace sector revenues reaching \$23 billion.

What we found

- Before 2010, Industry Canada had inadequate performance information to determine progress being made to achieve the Strategic Aerospace and Defence Initiative's objectives. Since 2010, the Department has made improvements and now collects and consolidates sufficient information to allow it to determine progress against the program's objectives. However, the Department has not followed through on its commitments to report publicly on the program's results. As well, the Department will need to follow through on commitments to collect additional performance information so that it can complete its planned evaluation of the program in 2016–17. For the Bombardier CSeries Program, the Department has not collected all documents required by the contribution agreements to determine progress toward the program's objectives, so it has a more limited picture of the program's performance.
- Industry Canada has managed most aspects of these transfer payment programs appropriately, using a control framework that is reasonable—for example, it reviews recipients' claims and progress reports before issuing payments. As well, the Department funded only recipients that met program eligibility requirements. It also undertook a detailed review of proposed projects before signing contribution agreements with recipients. However, the Department did not define the appropriate level of monitoring and reporting for the different levels of risk assigned to the projects and for the amount of funding provided to individual recipients.
- In cases where contributions under the Defence Industry Productivity Program and Technology Partnerships Canada were repayable, the majority of repayments we examined were obtained by Industry Canada on time.

The Department has responded. The Department agrees with our recommendations. Its detailed responses follow the recommendations throughout the chapter.

Introduction

6.1 The aerospace sector in Canada includes commercial aerospace; military aerospace; aircraft maintenance, repair, and overhaul services; and the development, deployment, and operation of space assets. Aerospace companies are important contributors to the Canadian economy. The National Research Council Canada reported that Canada's aerospace sector ranks as the fifth largest in the world as of 2008, with total revenues of \$23 billion.

6.2 Many countries provide financial support to their own aerospace sector. The Government of Canada, which sees the aerospace sector as crucial to Canada's economic development, sovereignty, national security, and public safety, has provided financial support to the sector continuously since the 1950s. The government credits this support with contributing to a viable Canadian aerospace industry that is internationally competitive in areas such as aircraft engines, landing gear, and aircraft production.

6.3 The aerospace sector is research and development intensive, and often there is a long period of time between when a new technology is conceptualized to when it is produced. Providing financial support is not without risks—the government recognizes that not all projects will succeed, technically and commercially, and therefore not all projects will generate the original expected outcomes. Economic change, global competitiveness, and changing market conditions all add an element of risk. The federal government's approach—sharing risks and rewards—is intended to encourage private sector investment.

Industry Canada uses transfer payments to support the aerospace sector

6.4 Industry Canada is the lead department for science within the federal government. Its mandate is to encourage the fullest, most efficient, and most effective development and use of science and technology. Industry Canada also works on making Canadian industry more productive and competitive in the global economy.

6.5 Industry Canada delivers the Strategic Aerospace and Defence Initiative (SADI), which is the federal government's second-largest research and development direct spending program. SADI was launched in 2007 as an ongoing program to support private sector industrial research and pre-competitive development in Canada's

aerospace, defence, security, and space industries through repayable contributions to support projects. SADI has three objectives:

- to encourage strategic research and development that will result in innovation and excellence in new products and services;
- to enhance the competitiveness of Canadian aerospace and defence; and
- to foster collaboration between research institutes, universities, colleges, and the private sector.

6.6 Examples of supported industrial research include the development of innovative aircraft simulator systems and research to develop a safe and effective alternative to the use of cadmium in the electroplating process for aerospace applications. Examples of supported pre-competitive development include projects to improve the reliability and performance of landing gear systems and projects to develop lighter aircraft engines with more power, better fuel consumption, and improved durability.

6.7 As of 1 April 2012, a total of 22 companies signed 25 unconditionally repayable or conditionally repayable contributions (Exhibit 6.1) for strategic research and development projects. Under SADI contribution agreements, Industry Canada disburses funds to recipients over multiple years; SADI contributes up to 40 percent of eligible costs of funded projects. Funds are typically repayable over 15 years after the end of the project. The Department authorized just under \$825 million in contributions (funds disbursed as of 1 April 2012 were almost \$325 million). Within Industry Canada, the Industrial Technologies Office manages this program.

Exhibit 6.1 What is a contribution?

A **contribution** is a transfer payment subject to performance conditions specified in a funding agreement. A contribution is to be accounted for and is subject to audit.

A **repayable contribution** is a contribution whereby the recipient is expected to repay all or part of the amount, or the government expects to receive a financial return. The terms may specify a date or dates for repayment, or may prescribe the particular time(s) or circumstance(s) that will determine repayment.

Repayable contributions are further classified as unconditionally repayable and conditionally repayable. **Unconditionally repayable contributions** must be repaid without qualification. The contribution agreement contains specific repayable terms.

Conditionally repayable contributions are contributions, all or part of which are repayable, if conditions specified in the contribution agreement come into being.

Source: Treasury Board of Canada Secretariat

6.8 The Department also manages two conditionally repayable contribution agreements with Bombardier Inc. in support of research and development projects associated with the Bombardier CSeries Program. The contributions are intended to encourage research and development that will result in the development of new commercial aircraft technologies, including the new CSeries commercial jet. Expected results include encouraging and leveraging private sector investment, as well as maintaining and growing the technology base and technological capabilities of Canadian aerospace firms. A total of \$350 million in funding was authorized for the fiscal years 2008–09 to 2014–15 (funds disbursed as of 31 March 2012 were just under \$203 million). The Aerospace, Defence and Marine Branch of Industry Canada manages this program.

6.9 Finally, Industry Canada manages the Defence Industry Productivity Program (DIPP) and Technology Partnerships Canada (TPC). Both programs are in the repayment phase, which is the final phase for these programs. The objective of DIPP, which ran from 1959 to 1995, was to develop and maintain defence-related industries capable of competing in domestic and export markets. Recipients received \$2 billion from 1985 onwards. Fifty-five percent of these DIPP contribution agreements were repayable.

6.10 DIPP was replaced by TPC, which ran from 1996 to 2006. Its mandate was to invest in projects with firms to support technological development that fostered innovation, commercialization, sustainable development, and increased investment. Industry Canada has disbursed \$3.1 billion in repayable contributions to recipients. All TPC contribution agreements were repayable.

Focus of the audit

6.11 We examined whether Industry Canada had sufficient information to determine if the Strategic Aerospace and Defence Initiative (SADI) and the Bombardier CSeries Program were meeting their stated objectives, and whether these programs were managed according to the key requirements of the Treasury Board Policy on Transfer Payments and the terms and conditions of the programs. Our audit included the 24 SADI agreements signed prior to 1 March 2012 and the 2 Bombardier CSeries Program agreements. We also examined whether the Department collected amounts that recipients were to repay under two legacy programs—the Defence Industry Productivity Program and Technology Partnerships Canada. Our audit examined Industry Canada's performance; we did not audit recipients of government

funding. A separate audit on transfer payment program reforms appears as Chapter 2 of this report, Grant and Contribution Program Reforms.

6.12 Audit work for this chapter covers the period from 1 January 2007 to 1 June 2012. More details on the audit objectives, scope, approach, and criteria are in **About the Audit** at the end of this chapter.

Observations and Recommendations

Measuring progress on objectives

6.13 The Policy on Transfer Payments requires that departments establish a performance measurement strategy at the time of program design and that the strategy be maintained and updated to support the evaluation or review of the program's relevance and effectiveness. A performance measurement strategy guides program and corporate decision making. It also helps ensure there is adequate and relevant information to support continuous monitoring. Industry Canada committed to developing performance measurement strategies for both the Strategic Aerospace and Defence Initiative (SADI) and the Bombardier CSeries Program to measure whether these programs are meeting their objectives.

6.14 Measuring whether overall program objectives are met requires that performance information is collected from recipients at the individual project level. The terms and conditions for both SADI and the Bombardier CSeries Program require that contribution agreements with individual recipients contain provisions for them to submit periodic reports to Industry Canada so the Department can assess the progress of projects. These reports should include information on the achievement of project objectives, progress against performance milestones, and how the funds provided were used.

6.15 With the end of Technology Partnerships Canada in 2006, Industry Canada had an opportunity to incorporate lessons learned with respect to performance measurement and reporting into the design and delivery of its successor, SADI. The Department also committed to undertake multiple evaluations of SADI and to evaluate the Bombardier CSeries Program. Finally, for SADI, the Department committed to reporting publicly each year on contribution recipients, on program results and accomplishments, and on how approved projects met the assessment criteria—responding to its commitment to set new standards for transparency.

6.16 We sought to determine whether the Department

- put in place performance measurement strategies for SADI and the Bombardier CSeries Program to collect information;
- collected performance information on individual projects;
- evaluated Technology Partnerships Canada and fulfilled early evaluation commitments for SADI; and
- publicly reported each year on SADI contribution recipients, program results, and accomplishments.

Performance measurement strategies are in place

6.17 Industry Canada established performance measurement strategies for SADI and the Bombardier CSeries Program. These strategies are consistent with the main elements of a performance measurement strategy outlined in Treasury Board of Canada Secretariat guidance.

6.18 The SADI performance measurement strategy sets out an approach to measure SADI objectives (innovation, competitiveness, and collaboration) and includes performance indicators associated with program objectives and outcomes. For example, under the objective of innovation, indicators include research and development dollars invested leveraged per SADI dollars invested. It also includes project-specific outcomes, linked to program objectives, that may result from individual SADI projects. For example, new patent applications filed or granted are project-specific benefits under the innovation objective.

6.19 The Bombardier CSeries Program performance measurement strategy includes performance indicators such as the number and type of research and development positions maintained and created under the agreements, as well as the number and type of collaborations with research institutions, universities, and other companies.

6.20 These performance measurement strategies provide the Department with a plan for continuously monitoring and assessing program results; a means to collect the information to make informed decisions and take appropriate, timely action with respect to programs; a means to provide effective and relevant departmental reporting on programs; and a way to ensure that credible and reliable performance data is collected to support evaluations of the programs.

The Department is now collecting more performance information on individual projects

6.21 A contribution is a transfer payment subject to performance conditions specified in a funding agreement. The Treasury Board Directive on Transfer Payments specifies that agreements should include a description of the purpose of the contribution and the activities, project, or initiative being funded and the results that the recipient is to achieve. The results expected should be within the reasonable control of the recipient and should be stated at a level of detail that will support accountability and performance measurement. Agreements should also include a description of the information that will be requested from recipients for financial and performance reporting, including information on results achieved to support the program's performance measurement strategy and departmental reporting. The contribution agreement constitutes the entire agreement between the parties.

6.22 Program and project objectives. We examined whether contribution agreements clearly set out project objectives and whether these objectives corresponded to overall program objectives. We also examined Industry Canada's monitoring of recipients through reporting requirements specified in the contribution agreements—progress reports, site visits or progress meetings, and annual performance reports. We wanted to determine if information was captured on the progress of projects, their results, and how the projects contributed to achieving overall program objectives.

6.23 For SADI, we did not find a clear link between the project-level objectives contained in many of the 24 contribution agreements with recipients and SADI's overall program objectives. In most cases, the contribution agreements did not include a clear description of project-specific objectives that were linked to overall program objectives. In our opinion, this makes it more difficult for Industry Canada to determine and demonstrate the extent to which individual projects are contributing to achieving the overall SADI objectives.

6.24 Anticipated outcomes and benefits. We noted that the Department made improvements in later SADI agreements to ensure a clearer link between the project-level objectives contained in the individual agreements and the overall SADI program objectives. In addition, six contribution agreements signed from April 2010 onwards contained a specific section on the projects' anticipated outcomes and benefits, which corresponded to overall program objectives. We were encouraged by this important improvement. Contribution agreements document requirements the recipients must meet in return for receiving funds from the federal government.

6.25 Including anticipated outcomes and benefits in contribution agreements should allow for easier reporting on progress and results achieved by the projects. It may also help the Department collect the information it needs to report on the achievement of program objectives. We noted that in response to an internal review on collaboration in 2011, the Department agreed to make collaboration expectations and reporting requirements contractually explicit in the contribution agreement template. Industry Canada's officials informed us that the Department will continue the practice started in 2010 of including the anticipated outcomes and benefits for individual projects in the contribution agreements.

6.26 Monitoring and reporting. Industry Canada included several monitoring and reporting requirements in the SADI contribution agreements. The agreements require that project recipients prepare quarterly or monthly progress reports to demonstrate whether projects are progressing according to the work plans outlined in the contribution agreements. The agreements also specify that annual site visits or progress meetings must be carried out to monitor what is happening “on the ground.” All of the contribution agreements include a clause that requires recipients to provide information on the project’s outcomes if the Department requests it. As well, the first 17 contribution agreements that were signed contained a specific requirement for companies to prepare an annual performance report that included information on projects’ progress toward meeting anticipated project outcomes and benefits. The last 7 contribution agreements instead contained a requirement for recipients to participate annually in preparing and updating benefits reports to document the outcomes of the project and to assist in communicating the value and performance of SADI.

6.27 We found that recipients provided all of the progress reports that the contribution agreements required. Some reports were detailed and provided specific information not only on technical progress but also on the projects’ outcomes and benefits, while other reports did not clearly state the outcomes and benefits that were achieved. This was particularly the case for progress reports that were prepared before 2010. We saw that there was generally more information on project outcomes and benefits in the progress reports after the Department specifically asked recipients in contribution agreements for this type of information. We noted that Industry Canada officials reviewed the progress reports and contacted recipients for more details and clarification when needed.

6.28 We saw evidence that almost all of the SADI site visits and progress meetings that the contribution agreements required took place. However, they were not always well documented in the project files, which makes project monitoring more difficult over time. We noted that the more recent agreements require preparing meeting minutes with recipients, which could lead to better documentation of meetings in the future.

6.29 We verified whether Industry Canada obtained annual performance reports as required by the contribution agreements and whether these reports included information on project outcomes and benefits. We found that Industry Canada did not request these reports before 2010. The Department therefore lost an opportunity to collect some of the information it needed on how the projects were meeting SADI's program objectives. This information was needed to meet its requirement to report publicly each year on contribution recipients, and on overall SADI program results and accomplishments. The Department stated that it collected some of this information through other mechanisms, including progress reports and site visits.

6.30 For the 2010–11 fiscal year, departmental officials prepared annual project benefits reports for each project, outlining progress and achievements related to key performance indicators. The reports indicated that some projects were not at a stage where all of the indicators for assessing progress on outcomes could be measured.

6.31 For the Bombardier CSeries Program, the project progress reports contained limited information on outcomes and benefits, such as collaboration with research institutions or universities. As a result, the Department cannot rely solely on progress reports as a source of performance information. We also found that although the Department conducted site visits, it did not document them well. Annual progress reports were required by the contribution agreements, but Industry Canada did not request them. The Department told us that while these required reports were not received, it did use other sources of information to monitor progress. However, without the documentation required under the contribution agreement, the Department has a more limited picture of the program's performance.

6.32 Progress reports, annual site visits or progress meetings, and annual performance reports are important tools for Industry Canada to monitor whether recipients are meeting project commitments and whether the projects are meeting program-level objectives. Since Industry Canada did not consistently collect comprehensive performance information through these monitoring mechanisms

before 2010, determining whether projects are meeting program-level objectives and undertaking program-level evaluations may be more difficult than if the Department had complete performance information on each project. With respect to SADI, since 2010, the Department has made improvements and now collects and consolidates sufficient information to allow it to determine progress against objectives.

6.33 Recommendation. Industry Canada should ensure that monitoring and reporting requirements set out in its contribution agreements are fully met and documented.

The Department’s response. Agreed. The Department will ensure that the monitoring and reporting requirements of contribution agreements are fully met and documented.

6.34 Recommendation. Industry Canada should ensure that future contribution agreements it signs with recipients specify project-specific objectives and identify anticipated outcomes and benefits that are aligned with the Strategic Aerospace and Defence Initiative program objectives.

The Department’s response. Agreed. The Department will continue the practice, started in 2010, to include in its contribution agreements a section specifying project-specific objectives and identifying the anticipated outcomes and benefits of the project in order to demonstrate clearly their alignment with the Strategic Aerospace and Defence Initiative’s objectives.

The Department has been slow to measure progress against program objectives

6.35 We examined the Department’s efforts to evaluate Technology Partnerships Canada (TPC) to help inform performance measurement for SADI. We found that in 2003, Industry Canada conducted an evaluation of TPC that focused on program design and delivery, which provided the Department with important information about operational issues. The evaluation assessed performance over the first six years of TPC’s operations, from 1996 to 2002.

6.36 We found that a final evaluation of TPC’s program effectiveness—including of the program’s longer-term technological, economic, and societal outcomes—has not been done. The Department had committed to completing this evaluation in 2011. The Department’s multi-year evaluation plan, dated May 2012, commits the Department to complete an evaluation of TPC in 2015–16. However, this means the Department is not yet in a position to integrate lessons

learned from a final evaluation of TPC to potentially improve performance measurement for SADI.

6.37 For SADI, we found that Industry Canada has delayed and cancelled some of its evaluation commitments, potentially missing out on early improvement opportunities. The initial implementation review, due in the 2008–09 fiscal year, was intended to assess program implementation and the performance measurement strategy. It was not completed until October 2010, at which point the program was already well established. In addition, it addressed only the development of the performance measurement strategy; program implementation was not addressed.

6.38 Departmental officials cancelled the interim evaluation of the achievement of SADI’s intended immediate outcomes, due in 2009–10. This decision, which the Departmental Evaluation Committee approved, was made because the Department felt there would have been little value in undertaking such an evaluation at that time, given the number of projects in their early stages.

6.39 In October 2011, the Department reported a review of the status of collaboration between project recipients and post-secondary institutions (one of SADI’s objectives). As well, an evaluation of SADI was reported in January 2012. The evaluation assessed program relevance and aspects of performance to date, including investments in research and development, collaboration, and the development of products, processes, and services. We noted that Industry Canada’s multi-year evaluation plan has committed the Department to completing another evaluation of SADI in 2016–17. This additional evaluation effort is required for a full assessment of whether program objectives are being met, including whether longer-term outcomes are being realized.

6.40 For the Bombardier CSeries Program, no implementation review or evaluation has been carried out. An implementation review was recommended in the performance measurement strategy to be completed in 2009–10. The Department’s May 2012 multi-year evaluation plan commits to an evaluation of the Bombardier CSeries Program to be reported in 2015–16 as per the direction provided to Industry Canada when the program was approved. However, this means that no formal assessment of the program is planned before all funding has been disbursed. As a result, the Department is missing an opportunity to make potential timely improvements to the program.

6.41 Since 2007, Industry Canada has authorized assistance of almost \$1.2 billion in contributions through SADI and the Bombardier CSeries Program (almost \$528 million has been disbursed as of April 2012). Implementation reviews and evaluations are intended to establish whether the programs are on track to meet program objectives. The Department has been slow to meet its evaluation commitments. For SADI, the Department decided to delay or cancel its commitments because it determined that it was too early to measure results. However, without the benefit of this performance information, it is more difficult for the Department to demonstrate progress against program objectives.

6.42 Recommendation. Industry Canada should ensure that its planned evaluations of Technology Partnerships Canada, the Strategic Aerospace and Defence Initiative, and the Bombardier CSeries Program are carried out to allow the Department to measure progress against program objectives. These evaluations should be reported within the time frames the Department has committed to in its multi-year evaluation plan.

The Department's response. Agreed. The Department will evaluate its transfer payment programs in accordance with its multi-year evaluation plan.

The Department's public reporting on SADI achievements has been limited

6.43 The Department committed to report publicly each year on contribution recipients, program results and accomplishments, and how approved projects met the assessment criteria. This was to ensure program transparency. As well, the SADI performance measurement strategy requires that, once a year, the Department consolidate performance information that is collected on each project into an Annual Program Benefits Report. The report's aim is to communicate clearly the results the program has achieved relative to the established objectives and outcomes.

6.44 Although this requirement has been in place in one form or another since 2007, we found limited reporting to meet this commitment. In 2009, Industry Canada publicly released Program Highlights 2007–09, a document that contained limited information on program achievements. In 2012, the Department completed an internal report covering the 2010–11 fiscal year, which provided some information on how selected projects are meeting SADI objectives. However, this report was not released publicly. Our review of Industry Canada's departmental performance reports and the Department's website found few references to SADI results and accomplishments.

6.45 Recommendation. Industry Canada should ensure that it meets its commitment to report publicly each year on how approved projects met the Strategic Aerospace and Defence Initiative assessment criteria on contribution recipients and on program results and accomplishments.

The Department's response. Agreed. Industry Canada will augment the information already available on its website to include additional information in these areas, although the commercially sensitive nature of the projects will continue to limit the amount of information that can be lawfully released to the public. The Department will report this information by the end of December 2012 for all projects approved by 2011–12, and annually thereafter.

Managing aerospace transfer payments

6.46 Funds that Industry Canada transfers to recipients under the Strategic Aerospace and Defence Initiative (SADI) and the Bombardier CSeries Program entail a significant commitment of federal government resources. The government has committed to ensuring that transfer payment programs are delivered and managed fairly, accessibly, and effectively.

6.47 The Treasury Board Policy on Transfer Payments and its associated Directive and Guidelines specify the requirements for departments to follow in managing transfer payments. These documents require, among other things, that Industry Canada

- identify eligible recipients along with the nature and type of initiatives that will be considered eligible under the transfer payment program;
- ensure that monitoring and reporting requirements reflect the risks specific to the amount of funding and the risk profile of the recipient; and
- ensure that cost-effective oversight, internal control, performance measurement, and reporting systems are in place.

6.48 For SADI and the Bombardier CSeries Program, we sought to determine whether Industry Canada

- ensured that only recipients eligible for funding under program terms and conditions of programs received funding (we did not examine the application process itself),
- ensured that recipient monitoring and reporting requirements were proportionate to the risk profile of individual recipients and to the level of funding,

- assessed recipients' claims and progress reports before issuing payments, and
- established a management framework for the control and oversight of transfer payments.

The Department funded recipients that met program eligibility requirements

6.49 The program terms and conditions for both SADI and the Bombardier CSeries Program define eligible recipients, activities, and costs. We examined whether Industry Canada conducted sufficient analysis to determine the eligibility of each of the 24 SADI projects and the 2 Bombardier CSeries Program projects before signing agreements with recipients.

6.50 For the 24 SADI projects and the 2 Bombardier CSeries Program projects, we found that before approving the projects, the Department conducted eligibility reviews, reviews of project feasibility, and reviews of companies' ability to deliver on proposed technological, social, and economic benefits. Overall, we found that these reviews were consistent with the Department's guidelines.

Monitoring and reporting requirements in contribution agreements do not reflect the level of risk or amount of funding

6.51 The Policy on Transfer Payments and its associated Directive emphasize a risk-based approach to recipient monitoring and reporting. Departmental officials are responsible for ensuring that the requirements placed on recipients are proportionate to the risk level of the project. In particular, monitoring and reporting requirements in the agreements should reflect the level of funding and the risk profile of the recipient. For the 24 SADI projects and the 2 Bombardier CSeries Program projects, we reviewed whether the Department assessed risks to determine the level of monitoring and reporting requirements to be included in the individual contribution agreements.

6.52 We found that a risk analysis was completed for all 24 SADI projects. The analysis for each project included an assessment of technological capability and feasibility risks as well as managerial, financial, and market risks. The projects were then assigned an overall risk level. The analyses were detailed, incorporating the views of departmental officials and, on occasion, external experts. The Department identified only one project as low risk and one as medium-low risk. Conversely, for the Bombardier CSeries Program projects, although a risk analysis was completed that included a description of various risks, an overall rating was not assigned.

6.53 As well, we found that the Department has not defined the appropriate level of monitoring and reporting for the different risk ratings and amount of funding. The Department uses a standard template to draft contribution agreements, which means that all agreements include the same monitoring and reporting requirements regardless of the assessed risks. Departmental officials informed us that the standard frequency for recipients to submit claims and progress reports is quarterly, but that if recipients ask to submit them monthly, the Department will accept them. In our view, defining such levels would help the Department better target its monitoring and reporting efforts.

6.54 We found that monitoring and reporting requirements specified in the contribution agreements with recipients were not proportionate to the levels of risk assigned to the SADI projects. For example, the monitoring and reporting requirements in the contribution agreements for three projects identified as high risk were mostly the same as for the two projects identified as low risk and as medium-low risk. Departmental officials told us that the wording of the contribution agreements provides them with the flexibility to request more information from recipients if risks change.

6.55 As well, we found that there was no correlation between the level of funding and the level of monitoring and reporting requirements outlined in the contribution agreements. This is important, given that the funding provided through the agreements ranged from just under \$300,000 to \$300 million. For example, for claims monitoring, monthly claims and monthly progress reports were required for 3 of the 24 SADI projects. The projects were for significantly different amounts, indicating that the level of funding was not a factor that determined the level of monitoring and reporting. The other 21 agreements required quarterly claims and progress reports, even though their respective risk ratings ranged from low to high.

6.56 We observed that the Department has recently been more proactive in revisiting its risk ratings for the SADI projects. It reviews ratings on a quarterly basis and has revised the overall risk levels for projects as required. In 2009, the Department established the Industrial Technologies Office (ITO) Risk Management Committee, which is responsible for overseeing ITO's efforts to manage project and program risks. We found that the Committee discussed risks for individual projects and proposed mitigation measures. However, we did not find actions taken in response to be well documented.

6.57 Having monitoring and reporting requirements in the contribution agreements that are proportionate to risks is important, because these mechanisms could allow Industry Canada to identify potential problems in higher-risk projects earlier on. This may enable the Department to take corrective action more quickly than would otherwise be possible. Since we found that monitoring and reporting requirements are not proportionate to project risks, efficiencies could be missed, unnecessary burdens may be placed on recipients, and departmental resources may not be well targeted.

6.58 Recommendation. The Department should document its approach to risk management, specifying the appropriate levels of monitoring and reporting to be used, proportionate to the risks of the project, the value of funding in relation to administrative costs, and the risk profile of the recipient.

The Department's response. Agreed. The Department will document its risk management approach for the Strategic Aerospace and Defence Initiative to demonstrate more clearly the rationale behind the specific approaches taken to manage the various risks inherent in funding aerospace research and development projects. The Department will document its overall practices in this regard by the end of December 2012.

The Department reviewed recipient claims and progress reports before issuing payments

6.59 Section 34 of the *Financial Administration Act* requires that the responsible departmental officer must certify that the recipient is entitled to the payment before a payment is made. The contribution agreements for SADI and the Bombardier CSeries Program projects require that a progress report be submitted with claims. We verified whether the Department reviewed progress reports and claims before issuing payments.

6.60 We found that the Department has a process in place to verify claims that recipients submitted. This process is set out in its Verification of Claims Policy, which defines the roles and responsibilities of officials.

6.61 We examined selected claims made under four SADI agreements and both Bombardier agreements and found that Industry Canada officials reviewed them and the progress reports before the Department released payments to recipients. We found that through their detailed verification of claims, officials determined that some costs were not eligible. For SADI, assessments of progress reports were documented.

However, for the Bombardier CSeries Program, assessments of the progress reports were not documented. We observed that an authorized departmental officer certifies that the recipient is entitled to payment before funds are released.

6.62 Industry Canada has a multi-year recipient audit plan for financial audits of SADI recipients. The Department can also initiate other audits of recipients when it determines they are necessary.

A management control framework is in place to support transfer payments

6.63 The Treasury Board Policy on Transfer Payments requires departments to ensure that cost-effective oversight, internal control, performance measurement, and reporting systems are in place to support the management of transfer payments. The Policy further requires departments to establish reasonable and practical service standards for transfer payment programs. As Industry Canada administers close to 30 transfer payment programs of various sizes, ensuring that its management framework is current and relevant is important.

6.64 We examined three elements of the Department's management framework for the control and oversight of SADI and Bombardier transfer payments:

- departmental policies and procedures setting out requirements for control and oversight,
- information and reporting systems to manage and track agreements, and
- service standards for transfer payment programs.

6.65 Policies and procedures manuals. The Department has a Programs Policies Manual and a Programs Procedures Manual to provide guidance to departmental employees delivering programs. Both manuals predate the 2008 Policy on Transfer Payments. We found that Industry Canada has not finished reviewing the manuals to determine if they adequately reflect the current Treasury Board requirements for managing transfer payments.

6.66 In 2008, the Treasury Board of Canada Secretariat encouraged departments to establish Departmental Action Plans to improve the delivery and efficiency of transfer payments. Industry Canada told us it did not develop a formal action plan since it did not consider this to be a requirement. Starting in 2010, the Department prepared progress reports on its transfer payment reform activities. Updating internal policies and procedures would have been a first step toward aligning

programs with the revised Policy on Transfer Payments. We found that the Department has not yet completed its update to internal policies and procedures manuals and that this activity was not part of the progress reports. Having a work plan in place to guide actions that needed to be taken to make changes required by the 2008 Policy on Transfer Payments could have helped the Department to ensure that internal policies and procedures manuals were updated on a timely basis. Our recommendation at paragraph 70 addresses this finding.

6.67 Information and reporting systems. The Contribution Management Information System (CMIS) is the Department's primary system for monitoring and managing agreements. Additional systems were created because the Department found that CMIS was not meeting all of its needs. For example, the Industrial Technologies Office created a Data Warehouse to capture performance information, since this function is not available through CMIS.

6.68 In 2008, an internal audit noted that limitations to CMIS diminished its usefulness as a tool to support program staff in managing contribution agreements. The audit recommended that the Department articulate a vision and transition strategy for a new management system for departmental transfer payments and ensure that any replacement system include the ability to track and report on program benefits. The Department agreed with the recommendation, saying that the design of a new replacement system would include the ability to track program benefits and to produce reports on these benefits.

6.69 However, the Department has not yet identified a replacement system for CMIS. The Department obtained an additional assessment of CMIS in March 2012. The assessment recommended taking steps to sustain the existing CMIS platform for the next six years and proposed an approach to phase in new components to extend the existing CMIS system capability.

6.70 Recommendation. Industry Canada should establish a plan with deadlines to ensure that its management control framework for transfer payments, including its policies, procedures, and electronic systems, is consistent with requirements set out in the Policy on Transfer Payments and is meeting the needs of the Department.

The Department's response. Agreed. The Department will develop a plan with deadlines by November 2012.

6.71 Service standards. Industry Canada established service standards for managing SADI as the Policy on Transfer Payments required. The Department has assessed its performance in managing

SADI through three service standards (Exhibit 6.2). We noted that while the Department did not establish formal service standards for the Bombardier CSeries Program, it stated that it had an informal standard of 30 days for the processing of claims. Because this was not a formal standard, we did not review the Department's performance against it.

Exhibit 6.2 Strategic Aerospace and Defence Initiative (SADI) has created service standards to assess its performance

Application processing time

- Complete the review of a proposal and provide recipients with a funding decision within six months of receiving a complete project application

Claims processing time

- Process completed claims and release payments for contribution agreements in good standing within 45 calendar days

Application assistance response time

- Respond to requests for assistance with a project application within one business day

Source: Industry Canada

6.72 As of April 2010, the Department reported publicly on whether it met the service standards for SADI. The latest report, for the fourth quarter of 2011–12, states that 100 percent of applications were processed within six months, that 100 percent of application assistance requests were answered within one business day, and that 100 percent of completed claims were released for payment within 45 calendar days.

6.73 We compared the Department's reporting against the 45-calendar-day standard for processing claims for payment as part of our audit. In our review, which encompassed several quarters, we found that close to 70 percent of completed claims for SADI were processed within 45 calendar days. The Department explained this discrepancy by telling us that the service standard does not apply when the recipient takes more than 10 days to provide missing information; when an amendment is being negotiated to resolve a possible breach of the agreement; and when there is no payment due, such as in cases where funds are being held back pending project completion. However, taking this approach means the performance standard is misleading.

6.74 Recommendation. Industry Canada should revisit its methodology to measure and report the achievement of service standards for the Strategic Aerospace and Defence Initiative, in particular the claims processing time standard, to ensure that the results reflect actual performance.

Obtaining repayments from recipients

The Department's response. Agreed. Industry Canada will review the claims service standard for the Strategic Aerospace and Defence Initiative by the end of December 2012.

6.75 The Treasury Board Directive on Transfer Payments requires that contributions made to for-profit businesses that are intended to allow the businesses to generate profits or increase the value of their businesses are to be repayable. Departmental managers are responsible for ensuring that amounts repayable by or recoverable from recipients are recognized as debts due to the Crown, and that appropriate action is taken to recover these amounts.

6.76 Since 1996, Industry Canada has received \$767 million in repayments for Technology Partnerships Canada (TPC) and since 1985, it has received \$607 million in repayments for the Defence Industry Productivity Program (DIPP). As of May 2012, Industry Canada forecasted a total of \$1.5 billion in repayments from the TPC program and \$299 million in repayments from the DIPP over the next 10 years, if repayment conditions are triggered.

6.77 Repayments received from companies under TPC flow back into payments to companies under the Strategic and Aerospace Defence Initiative (SADI) and the Bombardier CSeries Program. The Department's ability to fund these projects depends partly on funds obtained through TPC repayments. If Industry Canada does not receive repayments from recipients, then it may not be able to pay claims to recipients under the current contribution agreements. This risk was noted in Industry Canada's Corporate Risk profile.

6.78 Within the Department, the Comptrollership and Administration Sector is responsible for contribution agreements when they enter the repayment phase. Repayment conditions and schedules are specified in the contribution agreements. However, due dates and amounts due can change as market realities change. For example, if a repayment amount is based on royalties from sales, it could be different from what had been forecasted. If the company does not meet the repayment conditions—for example, if it does not meet a sales revenue target—it does not have to repay the amount due.

6.79 We examined whether Industry Canada has policies and procedures in place to manage repayments and whether it ensures that funds due under TPC and DIPP are collected from recipients. This work included drawing a sample of agreements in the repayment phase to determine the actions the Department has taken to collect repayments due. We did not examine the process used by the

Department to determine whether the conditions triggering repayments were met.

The Department took appropriate steps to obtain repayments due

6.80 We found that, of the repayments we reviewed as part of our audit, the Department obtained most repayments on time. Our findings are summarized in Exhibit 6.3. As well, Industry Canada has a Repayable Contribution Policy, adopted in 1996. The Department has documented procedures to manage repayable contributions. We noted that Industry Canada has recently started updating the Repayable Contribution Policy and its procedures.

Exhibit 6.3 In most cases examined, repayments were received on time

| Summary of repayments review | Technology Partnerships Canada projects | Defence Industry Productivity Program projects |
|---|---|--|
| Projects | | |
| Number of projects examined | 41 | 10 |
| Number of projects in which conditions were met to trigger repayments | 32 | 10 |
| Repayments | | |
| Number of repayments due | 132 | 55 |
| Number of repayments received late | 52 | 11 |
| Repayment amounts | | |
| Funds repaid as of May 2012 (millions) | \$64.1 | \$21.0 |
| Forecasted repayments over next 10 years (millions) | \$275.8 | \$5.7 |

Source: Industry Canada

6.81 We reviewed a representative sample of 41 TPC repayable project contributions, comprising a total of about \$554 million in government funding, and a random selection of 10 DIPP repayable project contributions, comprising a total of about \$40 million. We conducted these reviews to determine if the Department monitored the repayment process and obtained repayments on time from 2007 to 2012.

6.82 For TPC, we found that for 32 of the 41 projects, conditions that triggered repayments were met for at least one payment period during 2007 to 2012. A total of 61 percent of repayments were

obtained on time. For DIPP, all 10 projects in our selection had at least one payment period where the conditions triggering repayment were met. A total of 80 percent of the repayments were obtained on time.

6.83 For repayments that were late, the Department took appropriate steps to obtain these payments. Actions taken included sending emails and letters to recipients reminding them that repayments were due. Officials told us that in cases where this communication does not result in repayments, files can be transferred to the Department's Loan Insurance and Recoveries Directorate for additional action.

6.84 In summary, Industry Canada has policies and procedures in place to manage repayments, and it ensures that funds due under DIPP and TPC are collected from recipients. We found that of the repayments we reviewed as part of our audit, the Department obtained most on time. For repayments that were late, the Department took appropriate steps to obtain these payments.

Conclusion

6.85 Before 2010, Industry Canada had inadequate performance information to determine progress being made to achieve the Strategic Aerospace and Defence Initiative's (SADI) objectives. Since 2010, the Department has made improvements and now collects and consolidates sufficient information to allow it to determine progress against objectives. For the Bombardier CSeries Program, progress reports contained limited information on outcomes and benefits. The Department did not request annual progress reports, required under the two contribution agreements, meaning it had a more limited picture of the recipient's performance.

6.86 We conclude that the Department has made improvements since 2010, but it needs to follow through on commitments to collect additional performance information. This is important so that the Department can report on progress against objectives as the projects mature. Planned evaluations of SADI, to be reported in the 2016–17 fiscal year, and of the Bombardier CSeries Program, to be reported in 2015–16, will rely on such information.

6.87 When it introduced SADI, the Department committed to increasing its level of transparency. However, the Department has not followed through on its commitment to report publicly each year on the program's results. As well, our review of Industry Canada's

departmental performance reports and its website found few references to SADI results and accomplishments.

6.88 Industry Canada has a management control framework in place to guide the way it manages these transfer payments. The Department carried out a detailed review of proposed projects before signing contribution agreements with recipients and funded only recipients that met program eligibility requirements. It also reviewed recipient claims and progress reports before issuing payments. However, the Department needs to make some improvements, including better documenting of its approach to risk management.

6.89 In cases where contributions under the Defence Industry Productivity Program and Technology Partnerships Canada were repayable, the majority of repayments we examined were obtained by the Department on time. The Department has documented procedures to manage repayable contributions, and has recently started updating these procedures.

About the Audit

All of the audit work in this chapter was conducted in accordance with the standards for assurance engagements set by The Canadian Institute of Chartered Accountants. While the Office adopts these standards as the minimum requirement for our audits, we also draw upon the standards and practices of other disciplines.

Objective

The objective of our audit was to determine whether Industry Canada has sufficient information to assess whether selected science and technology transfer payments to the aerospace sector were meeting their stated objectives and whether the Department managed these transfer payments in accordance with key requirements of the Policy on Transfer Payments.

Scope and approach

We looked at the Strategic Aerospace and Defence Initiative (SADI) and the Bombardier CSeries Program. We also examined whether Industry Canada collects repayments from recipients for contributions that are repayable. We looked at two legacy programs—Technology Partnerships Canada (TPC) and the Defence Industry Productivity Program (DIPP).

We reviewed the 24 contribution agreements under the SADI program signed as of 1 March 2012, as well as the 2 contribution agreements for the Bombardier CSeries Program. We looked to see if the Department had reviewed selected claims submitted under these agreements, but we did not audit the eligibility of the claims.

Separate selections of agreements were drawn for the TPC and DIPP programs. To complete the work on repayable contributions, for the TPC program, a representative sample of 41 agreements was selected from the total population of 188 active agreements. This sample size is sufficient to conclude on the population with a confidence level of 90 percent and a confidence interval of no more than 10 percent. For DIPP, a random selection of 10 agreements signed after 1985 was selected from a total population of 950 active agreements. We did not examine the process used by the Department to determine whether the conditions triggering repayments were met.

We analyzed contribution agreements, files, records, and reports. We interviewed Industry Canada officials who are responsible for the design and delivery of these programs. We also met with a number of companies that received contributions to obtain their views and opinions. Our audit examined Industry Canada's performance; we did not audit recipients of government funding.

Criteria

| Criteria | Sources |
|---|---|
| <p>To determine whether Industry Canada had sufficient information to assess whether selected science and technology transfer payments to the aerospace sector were meeting their stated objectives, and whether it managed these transfer payments in accordance with key requirements of the Policy on Transfer Payments, we used the following criteria:</p> | |
| <p>Industry Canada monitors recipients in accordance with program requirements, funding agreements, and the Transfer Payment Policy.</p> | <ul style="list-style-type: none"> • Terms and Conditions of the selected programs • 24 Strategic Aerospace Defence Initiative and 2 Bombardier CSeries Program funding agreements • Policy on Transfer Payments, Treasury Board, 2008 and 2000 • Directive on Transfer Payments, Treasury Board • <i>Financial Administration Act</i> • Guideline on Performance Measurement Strategy under the Policy on Transfer Payments, Treasury Board of Canada Secretariat |
| <p>Industry Canada has a performance measurement strategy or system that provides for appropriate collection of performance information at the level of individual recipients and at the transfer payment program level.</p> | <ul style="list-style-type: none"> • Policy on Transfer Payments, Treasury Board, 2008 and 2000 • Directive on Transfer Payments, Treasury Board • Guideline on Performance Measurement Strategy under the Policy on Transfer Payments, Treasury Board of Canada Secretariat |
| <p>Industry Canada uses performance information to modify programming as necessary and to demonstrate whether program results meet objectives.</p> | <ul style="list-style-type: none"> • Policy on Management, Resources and Results Structures, Treasury Board, 2010 and 2005 • Management Accountability Framework, Treasury Board of Canada Secretariat • <i>Financial Administration Act</i> • Policy on Evaluation, Treasury Board, 2009 and 2001 |
| <p>Industry Canada collects amounts repayable by, or recoverable from, recipients under agreements.</p> | <ul style="list-style-type: none"> • Policy on Transfer Payments, Treasury Board, 2008 and 2000 • Directive on Transfer Payments, Treasury Board • Guideline on the Directive on Transfer Payments, Treasury Board of Canada Secretariat • Accounting Standard 3.2—Treasury Board—Transfer Payments (Grants and Contributions) • Interest and Administrative Charges Regulations under the <i>Financial Administration Act</i> • Policy on Receivables Management, Treasury Board, 2002 |

Management reviewed and accepted the suitability of the criteria used in the audit.

Period covered by the audit

Audit work for this chapter covers the period from 1 January 2007 to 1 June 2012. Audit work for this chapter was completed on 17 July 2012.

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Appendix List of recommendations

The following is a list of recommendations found in Chapter 6. The number in front of the recommendation indicates the paragraph where it appears in the chapter. The numbers in parentheses indicate the paragraphs where the topic is discussed.

| Recommendation | Response |
|--|--|
| Measuring progress on objectives <p>6.33 Industry Canada should ensure that monitoring and reporting requirements set out in its contribution agreements are fully met and documented. (6.26–6.32)</p> | <p>Agreed. The Department will ensure that the monitoring and reporting requirements of contribution agreements are fully met and documented.</p> |
| <p>6.34 Industry Canada should ensure that future contribution agreements it signs with recipients specify project-specific objectives and identify anticipated outcomes and benefits that are aligned with the Strategic Aerospace and Defence Initiative program objectives. (6.22–6.25)</p> | <p>Agreed. The Department will continue the practice, started in 2010, to include in its contribution agreements a section specifying project-specific objectives and identifying the anticipated outcomes and benefits of the project in order to demonstrate clearly their alignment with the Strategic Aerospace and Defence Initiative's objectives.</p> |
| <p>6.42 Industry Canada should ensure that its planned evaluations of Technology Partnerships Canada, the Strategic Aerospace and Defence Initiative, and the Bombardier CSeries Program are carried out to allow the Department to measure progress against program objectives. These evaluations should be reported within the time frames the Department has committed to in its multi-year evaluation plan. (6.35–6.41)</p> | <p>Agreed. The Department will evaluate its transfer payment programs in accordance with its multi-year evaluation plan.</p> |

Recommendation**Response**

6.45 Industry Canada should ensure that it meets its commitment to report publicly each year on how approved projects met the Strategic Aerospace and Defence Initiative assessment criteria on contribution recipients and on program results and accomplishments. (6.43–6.44)

Agreed. Industry Canada will augment the information already available on its website to include additional information in these areas, although the commercially sensitive nature of the projects will continue to limit the amount of information that can be lawfully released to the public. The Department will report this information by the end of December 2012 for all projects approved by 2011–12, and annually thereafter.

Managing aerospace transfer payments

6.58 The Department should document its approach to risk management, specifying the appropriate levels of monitoring and reporting to be used, proportionate to the risks of the project, the value of funding in relation to administrative costs, and the risk profile of the recipient. (6.51–6.57)

Agreed. The Department will document its risk management approach for the Strategic Aerospace and Defence Initiative to demonstrate more clearly the rationale behind the specific approaches taken to manage the various risks inherent in funding aerospace research and development projects. The Department will document its overall practices in this regard by the end of December 2012.

6.70 Industry Canada should establish a plan with deadlines to ensure that its management control framework for transfer payments, including its policies, procedures, and electronic systems, is consistent with requirements set out in the Policy on Transfer Payments and is meeting the needs of the Department. (6.63–6.69)

Agreed. The Department will develop a plan with deadlines by November 2012.

6.74 Industry Canada should revisit its methodology to measure and report the achievement of service standards for the Strategic Aerospace and Defence Initiative, in particular the claims processing time standard, to ensure that the results reflect actual performance. (6.71–6.73)

Agreed. Industry Canada will review the claims service standard for the Strategic Aerospace and Defence Initiative by the end of December 2012.

Report of the Auditor General of Canada to the House of Commons

Matters of Special Importance

Main Points—Chapters 1 to 7

Appendices

Planning the Use of Professional Service Contractors

Grant and Contribution Program Reforms

Protecting Canadian Critical Infrastructure Against Cyber Threats

Transition of Ill and Injured Military Personnel to Civilian Life

Real Property—National Defence

Transfer Payments to the Aerospace Sector—Industry Canada

Long-Term Fiscal Sustainability—Finance Canada

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Long-Term Fiscal Sustainability—Finance Canada



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CHAPTER 7

Long-Term Fiscal Sustainability—Finance Canada



Performance audit reports

This report presents the results of a performance audit conducted by the Office of the Auditor General of Canada under the authority of the *Auditor General Act*.

A performance audit is an independent, objective, and systematic assessment of how well government is managing its activities, responsibilities, and resources. Audit topics are selected based on their significance. While the Office may comment on policy implementation in a performance audit, it does not comment on the merits of a policy.

Performance audits are planned, performed, and reported in accordance with professional auditing standards and Office policies. They are conducted by qualified auditors who

- establish audit objectives and criteria for the assessment of performance;
- gather the evidence necessary to assess performance against the criteria;
- report both positive and negative findings;
- conclude against the established audit objectives; and
- make recommendations for improvement when there are significant differences between criteria and assessed performance.

Performance audits contribute to a public service that is ethical and effective and a government that is accountable to Parliament and Canadians.

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Long-Term Fiscal Sustainability— Finance Canada

Main Points

What we examined

Long-term fiscal sustainability refers to a government's capacity to finance its activities and debt obligations in the future without imposing an unfair burden on future generations.

In its 2007 Budget, the federal government committed to publishing a comprehensive fiscal sustainability and intergenerational report aimed at providing "a broad analysis of current and future demographic changes and the implication of these changes for Canada's long-run economic and fiscal outlook." In 2011, the Office of the Auditor General encouraged the government to publish the long-term financial projections needed to fully assess the impact of the challenges facing the country and to inform Canadians.

We examined whether the Department of Finance Canada takes into account the impact of spending and tax measures on long-term fiscal sustainability before recommending new policies. We also examined how analyses of long-term fiscal sustainability are prepared and reported.

Audit work for this chapter was completed on 28 August 2012. More details on the conduct of the audit are in **About the Audit** at the end of this chapter.

Why it's important

The government faces many ongoing challenges that could impact Canada's long-term fiscal sustainability, such as changing demographics, climate change, and aging infrastructure. If the public debt were to grow faster than the economy for a long period, these challenges could make public finances unsustainable and reduce the living standard of future generations.

Long-term fiscal projections can help governments understand and protect the sustainability of public finances and respond more effectively to financial pressures in the future. Though long-term projections of fiscal sustainability are not predictions, they underpin fiscal sustainability and inform fiscal policy decisions. Understanding and considering the possible future consequences of fiscal decisions support sound economic development and the efficient use of available resources.

What we found

- Finance Canada officials prepare long-term fiscal analyses of spending and tax measures only if they consider it relevant to do so. Therefore, if the fiscal impact of measures being considered is not expected to change significantly relative to the size of the economy, the Department will not project the impact beyond five years. Although there are opportunities for improvements, we concluded that this approach, where officials use their professional judgment to determine whether the long-term fiscal impact needs to be considered, is reasonable. When officials do consider it relevant to perform analyses, they assess the long-term impact of individual measures on revenues or expenditures but do not always assess the impact on the budgetary balance and the public debt. Nor do they always project how the measures support or hinder long-term fiscal sustainability. Departmental officials rely on sometimes incomplete analyses of the long-term impact of measures when formulating recommendations.
- Regularly since 2010 and on occasion before that, Finance Canada has been providing the Minister of Finance with the results of fiscal sustainability analyses that project budgetary balance and public debt in the long term. However, the Department does not prepare these analyses—which indicate how budget measures will impact the fiscal position of the federal, provincial, and territorial governments—in time to inform budget decisions and before budgets are tabled in Parliament. For a given budget, the Minister is not informed of the overall long-term fiscal impact until months after the budget measures have been approved.
- While Finance Canada prepared a draft report in 2007 on the long-term fiscal sustainability analyses that the government committed to issuing that year, the analyses were not published; nor has any report on long-term fiscal sustainability been published since then. While long-term fiscal sustainability analyses have been regularly prepared since 2010, they have not been made public. This lack of reporting means that parliamentarians and Canadians do not have all the relevant information to understand the long-term impact of budgets on the federal, provincial, and territorial governments in order to support public debate and to hold the government to account. Many of the countries that are members of the Organisation for Economic Co-operation and Development (OECD) already publish reports on their long-term fiscal positions.

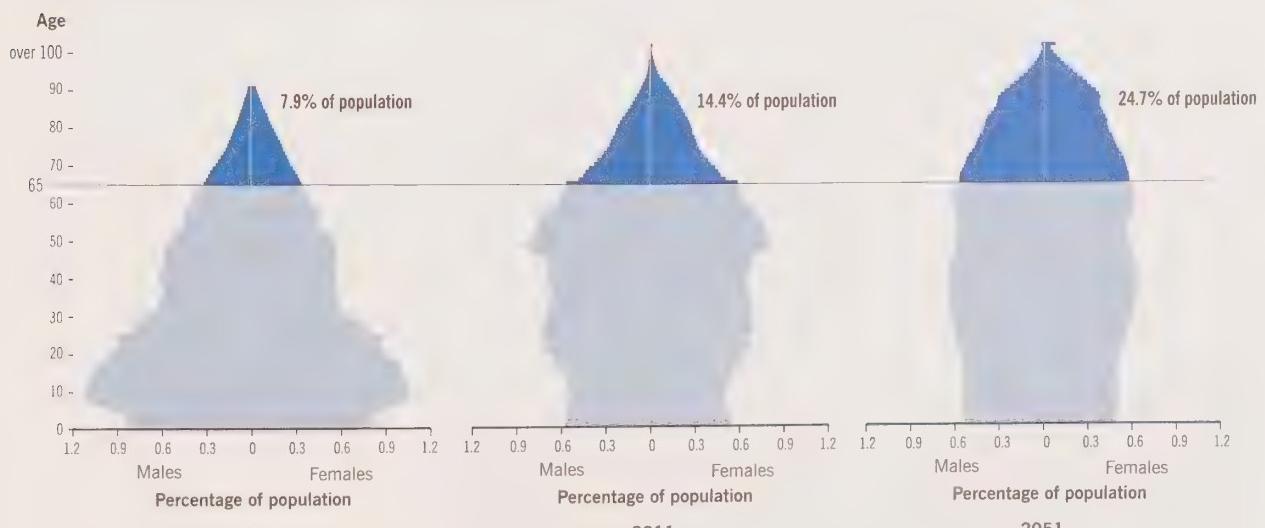
The Department has responded. The Department agrees with all of the recommendations. Its detailed responses follow the recommendations throughout the chapter.

Introduction

7.1 A number of significant risks could affect Canada's long-term fiscal sustainability, including demographic changes, climate change, and aging infrastructure. These challenges make it important for the government to understand the budgetary impact of existing policies and policy options on the country's long-term fiscal position and the sustainability of public finances. In this audit, we focus on how the Department of Finance Canada analyzes and considers long-term fiscal sustainability (which could be affected by demographic changes) in the process of making policy recommendations and how it reports long-term fiscal analyses.

7.2 Canada's population is aging rapidly (Exhibit 7.1). Canadians aged 65 and older now make up 14.4 percent of the population, compared with 13.3 percent in 2006. In 40 years, seniors will account for almost a quarter of the country's population. This demographic shift could weaken the fiscal position of governments by decreasing participation in the labour force, thus reducing potential economic growth as well as growth in government revenues. An aging population will also put upward pressure on health care costs and pensions. In this context, if interest charges on the public debt grow faster than the economy and unless revenues increase or spending levels decrease, the federal government could face an unsustainable budgetary position in the long run.

Exhibit 7.1 Seniors make up a growing proportion of Canada's population



Source: Adapted from Statistics Canada

7.3 Policy actions could be necessary to put public finances at the federal, provincial, and territorial levels on a solid footing, and to deal with the long-term spending and revenue pressures resulting from the aging population. The demographic changes require careful consideration because the macroeconomic outlook and fiscal conditions can rapidly deteriorate and jeopardize the long-term fiscal sustainability of governments. For example, the financial turmoil of 2008 heavily affected the long-term fiscal outlook of the federal, provincial, and territorial governments. Because of the impact of the financial turmoil on revenues and expenses, the federal government posted budgetary deficits of \$5.8 billion in 2008–09, \$55.6 billion in 2009–10, \$33.4 billion in 2010–11, and \$24.9 billion (estimated in Budget 2012) in 2011–12.

7.4 Long-term fiscal sustainability refers to the capacity of a government to finance its activities and its debt obligations in the future without placing an excessive burden on coming generations. Fiscal sustainability requires the growth of the economy to outpace government debt in the long run. Long-term fiscal analyses can help governments understand and protect the sustainability of public finances, and respond more effectively to possible future financial pressures. Exhibit 7.2 describes in more detail the concept of fiscal sustainability and how it can be analyzed and reported. It also explains the risks and limitations of long-term projections.

7.5 Long-term projections are not firm predictions. However, they underpin fiscal sustainability and provide guidance for fiscal policy decisions. Awareness and understanding of the future consequences of fiscal policies can foster sound economic development and the efficient use of available resources.

7.6 In 1998, the Office of the Auditor General published a study drawing attention to the inadequate information provided by the government to Parliament and the public concerning the implications of demographic trends and their potential impact on current fiscal decisions. The Department of Finance Canada responded that “presenting long-run fiscal projections to Parliament every year would serve only to detract attention from the important goal of debt reduction.”

7.7 In its 2007 Budget, the federal government committed to publishing a comprehensive fiscal sustainability and intergenerational report. As stated in the Budget, the report was to “provide a broad analysis of current and future demographic changes and the implication of these changes for Canada’s long-run economic and fiscal outlook.” The rationale for publishing a report on fiscal

sustainability was motivated by “the Government’s view that maintaining sustainable public finances at all orders of government is a critical condition to achieving intergenerational equity and strong and sustained economic growth.” The report was never published. The Department of Finance Canada last released a comprehensive analysis of the demographic challenge in an annex to the 2005 Budget.

Exhibit 7.2 Long-term fiscal sustainability analysis helps governments plan for the future

Sustainable public finances are required to achieve high and stable economic growth and to ensure that spending and taxation are distributed fairly across generations. Fiscal sustainability is about whether, based on current policy outlook, a government is headed toward excessive debt.

Fiscal sustainability has four dimensions:

Solvency: capacity to finance existing and probable future liabilities.

Growth: capacity to sustain economic growth over an extended period.

Stable taxes: capacity to finance future obligations without increasing the tax burden.

Fairness: capacity to provide to future generations benefits that are not less than benefits provided to current generations.

Long-term fiscal sustainability analyses may include baseline projections, fiscal gap analyses, and intergenerational accounting.

A **baseline projection** estimates revenues, spending, budget balance, and public debt at the end of a selected long-term period, using demographic, economic, and policy assumptions. This is the method most commonly used in jurisdictions abroad and the one used in this chapter. It involves critical economic assumptions, such as GDP growth, wages, productivity, and interest rates. By taking into account the fiscal impact of changing demographics, long-term fiscal analyses can provide insights into future budget conditions.

A **fiscal gap analysis** estimates the fiscal adjustment necessary to ensure that the present value of the primary balance (which is defined as the amount by which revenues, excluding investment income, exceed expenses, excluding public debt charges), given the present value of the debt, achieves a specific level of debt at the end of a selected period.

Generational accounting estimates the tax position of each age group over an extended period. This analysis focuses on the benefits that each age cohort will receive and the taxes it will pay.

Long-term fiscal sustainability analyses provide estimates, not predictions. Rather than exact fiscal forecasts, they are best estimates. The actual long-term fiscal position could be worse or better than projected. Among the reasons for the uncertainty of long-term projections are inappropriate fiscal modelling, poor demographic assumptions, wrong macroeconomic assumptions (including labour market participation, productivity forecasts, projected GDP, interest rates, and borrowing costs), and poor estimates of growth/decline in governments’ revenues and spending.

In addition, projections do not consider emergency spending to fund unforeseen events, such as financial crises, pandemics, wars, or natural disasters. Long-term fiscal projections assume no changes in policy. Finally, while a long-term analysis can project a situation in which governments start accumulating wealth and have no more debt, this situation is highly unlikely to occur. Future policy decisions could take advantage of projected surpluses by increasing spending through new or enriched programs, or by reducing taxes.

7.8 At the end of her 10-year mandate in 2011, former Auditor General Sheila Fraser expressed concern about the long-term fiscal pressures faced by the federal government. She encouraged the government to publish the long-term financial projections needed to fully assess the impact of the challenges ahead, and to inform Canadians and engage them in discussing the difficult choices that could eventually be required.

Focus of the audit

7.9 Our objective was to determine whether the Department of Finance Canada

- considered the long-term fiscal impact when analyzing and recommending spending and tax measures, and
- publicly reported information related to Canada's long-term fiscal sustainability.

7.10 We looked at the processes and tools used by the Department to prepare the fiscal impact of spending and tax initiatives with long-term budgetary consequences. For selected budget and fiscal update announcements, we examined whether the Department had prepared long-term fiscal sustainability analyses and had considered them in formulating recommendations. We also looked at the process used by the Department to project and publish sound analyses of overall long-term fiscal sustainability.

7.11 The audit examined how the policy decision framework takes into account long-term fiscal sustainability that could be affected by demographic factors. We did not examine how the decision-making process at the Department of Finance Canada takes into account the potential impact of climate change or aging infrastructure.

7.12 More details about the audit objectives, scope, approach, and criteria are in **About the Audit** at the end of this chapter.

Observations and Recommendations

Considering the long-term fiscal impact

7.13 Budget decisions need to take into account the long-term impact of a government's existing fiscal structure, as well as the interests and needs of future generations. If the needs of today's taxpayers are not properly balanced with those of tomorrow's, future generations may face a decline in living standards.

7.14 According to the International Monetary Fund and the Organisation for Economic Co-operation and Development (OECD), budgets should be prepared on the basis of realistic macroeconomic assumptions (for example, the growth rate of the economy, the rate of inflation, and interest rates), reasonable revenue projections, and realistic future costs of policies and programs. To recommend sound policy options with possible future impact, policy makers must have access to long-term fiscal analyses and projections.

7.15 We examined whether the Department of Finance Canada prepared sound analyses of the long-term impact of new spending and tax policies on fiscal sustainability before it recommended policy options. Such analyses need to take into account, when considered relevant, the future impact of spending and tax measures on revenues and expenditures, budgetary balances, and public debt. In a federation such as Canada, an analysis needs to include, when relevant, an assessment of the impact that federal decisions may have on provincial and territorial governments.

7.16 We also examined whether the Department of Finance Canada considered the results of these analyses when recommending spending or tax policy measures.

7.17 In this audit, we reviewed six spending and tax measures announced in federal budgets from 2007 to 2012:

- pension income splitting,
- the reduction of the goods and services tax (GST) rate,
- the maintenance of the GST/HST credit,
- the introduction of Tax-Free Savings Accounts (TFSAs),
- the new growth rate for the Canada Health Transfer (CHT), and
- the change in age of eligibility for Old Age Security (OAS).

7.18 We selected these measures because (unless policies change) they are long-lasting and they could have a significant long-term impact on federal, provincial, and territorial budgets and the fiscal outlook. Some programs or transfers (such as benefits for seniors and health care) will be affected by the aging population. Hence, performance of long-term fiscal sustainability analyses for the six selected measures could be relevant in view of the possible impact of these measures on the fiscal outlook. For each initiative, we examined whether and how the Department of Finance Canada assessed the projected impact on long-term sustainability, and whether it used analyses in formulating options and recommendations. We examined briefing notes and analyses prepared by the Department. We also interviewed officials from the Department.

The Department of Finance Canada has the capacity and tools to analyze the long-term fiscal sustainability of budget measures

7.19 Before determining whether the Department conducted analyses, we assessed the resources it had in place for doing so. We found that the Department has the analytical capacity and tools for projecting the long-term fiscal sustainability of measures before policy decisions are made. Qualified employees are available to prepare the analyses and projections. The Department has a number of tools at its disposal for assessing the impact of policy options:

- The **partial equilibrium accounting model** is the main tool used to produce long-term baseline projections and long-term analyses of fiscal sustainability. The fiscal variables used in these projections are based on underlying demographic and economic assumptions.
- The **static micro-simulation model** (T1 model) uses a sample of individual tax returns to simulate changes to the personal income tax system. To estimate the impact of possible tax changes on revenue, the model recomputes taxes payable using adjusted values.
- The **overlapping generation general equilibrium model** is a general equilibrium model designed to analyze fairness across generations. The model is based on the life-cycle theory of savings behaviour; this theory postulates that household members accumulate wealth during their working years by consuming less than their disposable income, and they consume out of their wealth during retirement. The model consists of three sectors: consumers, businesses, and government.

7.20 For preparing long-term projections of government debt and budgetary balances, the Department of Finance Canada uses the partial equilibrium accounting model. This model considers changes in revenues and expenses arising from foreseeable changes in the demographic and macroeconomic environments, particularly taking into account the impact of population aging.

Nominal gross domestic product—Gross domestic product (GDP) expressed in current dollars, that is, not adjusted for price variations.

Sensitivity analysis—Analysis that determines how small differences in the value of variables (such as GDP or interest rates) will affect the results of a projection.

7.21 The Department uses a number of assumptions in its analysis, such as interest rates and the components of growth in nominal gross domestic product—that is, productivity, population, and inflation. We found that the Department ensures that these assumptions are properly prepared and their reasonableness is verified. It compares the assumptions with those of other forecasters and also considers occasional peer reviews. We found that the Department uses sound analysis to project the growth rate of the various major components of government expenses, and then uses this data to project the fiscal balance in the long term. It performs sensitivity analyses of results when appropriate. Finally, we found that the Department has tools for projecting, when relevant, the fiscal impact of measures on provincial and territorial governments.

When formulating recommendations, the Department analyzes and considers the long-term fiscal impact only if officials judge the analyses to be necessary

7.22 We noted that departmental officials prepared analyses of the long-term fiscal sustainability of policy measures, when they considered them relevant, and they relied on the results to provide guidance for decisions. In its process for analyzing policies, the Department has no requirement to systematically analyze the long-term fiscal impact of policy measures. No agreement between officials is required to determine when or why such an analysis might be necessary. Officials indicated that if a proposed measure is not expected to have a significant fiscal impact relative to the size of the economy in the long term (that is, if it has no impact on the revenue-to-GDP ratio), they do not project the impact beyond five years. Also, while fiscal analyses project the long-term impact of individual measures on revenues and expenses, we found that some analyses do not always project the long-term impact that the measures will have on the overall budgetary balance and public debt. Further, the analyses do not always project how these measures support or hinder the long-term fiscal sustainability of the federal, provincial, and territorial governments. This means that at times the Department does not fully consider long-term impact when formulating recommendations. Our audit found the following results for the six measures we reviewed.

7.23 Pension income splitting. Under a personal income tax provision announced in the 2006 Tax Fairness Plan and included in the 2007 Budget, pensioners may split their eligible pension income with their spouse if certain requirements are met.

7.24 We found that the Department did not prepare analyses of the long-term fiscal sustainability of pension income splitting when the measure was proposed. Officials indicated that such an analysis was not relevant because the cost of the measure in the long run would be offset by a reduction in the pension income gap between spouses. The Department assumed that the proportion of families with two income earners would gradually increase, lessening the opportunity to split pension income. No analyses were available to support these assumptions. The Department now estimates that the cost of pension income splitting in forgone revenues was \$925 million in 2011 but will decline in coming years.

7.25 Goods and Services Tax and GST/HST credit. After an announcement in the 2007 Fall Economic Statement, the government reduced the goods and services tax from 6 percent to 5 percent in January 2008; earlier, in July 2006, it had reduced the tax rate from 7 percent to 6 percent. The government offers a credit to help persons with low or modest incomes offset all or part of the tax they pay—GST or, in applicable provinces, the GST part of the harmonized sales tax (HST). Despite the reduction in the tax, the credit to low-income earners was maintained as if the GST rate were still 7 percent. The second 1 percentage point reduction in the GST rate was estimated to cost \$6 billion in the 2008–09 fiscal year, the first full year of implementation of the 5 percent tax rate. The cost of maintaining the GST/HST credit as if the GST were still 7 percent was estimated at \$1.1 billion for 2008–09.

7.26 When the measures were announced, the federal government's budgetary position was considered to be strong in the long term because of sound economic and fiscal conditions. Department of Finance Canada officials determined that it was not necessary to perform long-term fiscal analyses of the tax rate reduction or GST/HST credit since the cost relative to GDP was not expected to grow. Senior management did not receive analyses of the long-term fiscal impact of these measures. Departmental officials told us that the long-term costs of the measures associated with the GST were included in the overall long-term fiscal sustainability analyses prepared for the Government of Canada and provided to senior management in 2007.

7.27 For our estimates, we replicated the economic and fiscal conditions of 2007, reducing the GST to 5 percent while maintaining the GST/HST credit at 7 percent. We found no substantial impact on the then sustainable long-term fiscal position of the federal government.

7.28 Tax-Free Savings Account. In the 2008 Budget, the government announced the Tax-Free Savings Account, for implementation starting in January 2009. This is a registered savings account that allows Canadians to accumulate investment income on a tax-free basis. Neither income earned within a TFSA nor withdrawals from it affect eligibility for federal benefits and credits that are based on the level of income of recipients. The cost of the measure was estimated at \$50 million in the 2009–10 fiscal year. More recently, the Department of Finance Canada estimated the cost to be \$220 million for 2011. The increase can be explained partly by the fact that the \$5,000 yearly contribution room is cumulative.

7.29 We found that the Department of Finance Canada estimated the long-term cost of the TFSA up to the year 2050, using the T1 micro-simulation model (see paragraph 7.19). The analysis included both the impact on personal income tax revenues and the benefits that depend on the income level of recipients. We found that the analysis accounted properly for a number of long-term factors, including demographic changes, annual increases in the TFSA contribution room, the interaction of the TFSA with unregistered assets and registered retirement savings plans, and the fact that income from capital gains would increase over time in TFSAs. While the analyses estimated the cost of the tax measure in the long term, they did not assess what impact it would have on the federal government's long-term budgetary balance and public debt. The Department of Finance Canada calculated the revenue impact on the provinces.

7.30 Canada Health Transfer. The Canada Health Transfer is the largest transfer from the federal government to the provinces and territories. In the 2011–12 fiscal year, it accounted for 47 percent of major transfers to other levels of government. According to the Department of Finance Canada, the CHT cash transfers will reach \$29 billion in the 2012–13 fiscal year and be made on an equal amount per capita basis in 2014–15.

7.31 The previous legislation governing the Canada Health Transfer was set to expire on 31 March 2014. In December 2011, the government announced changes to the CHT. The new legislation, introduced later, provides for a 6 percent yearly increase in the amount of the transfer through the 2016–17 fiscal year. Starting in the 2017–18 fiscal year, the

Moving average—A set of averages taken over a series of overlapping time periods. It strives to reduce short-term fluctuations and highlight more stable, longer-term trends.

transfer will grow in line with a three-year moving average of nominal GDP growth, with funding guaranteed to increase by at least 3 percent a year.

7.32 When the new CHT regime was announced, the Department of Finance Canada did not disclose the associated financial impact of the new growth rate of the health transfer or the way the change would affect the long-term sustainability of federal and provincial/territorial government finances. We sought to determine whether the Department had in fact assessed the long-term sustainability of this measure. The CHT is a significant expense relative to total federal government spending. If the CHT grew faster than the economy, it would put the long-term fiscal sustainability of the federal government at risk relatively quickly. From the viewpoint of the provincial/territorial governments, their public finances could face additional stress if health care expenditures increase over the coming decades as a result of population aging and other factors such as the price of technology.

7.33 We found that the Department of Finance Canada analyzed the long-term impact of different CHT options on the fiscal position of both the federal and provincial/territorial governments, using the partial equilibrium accounting model (see paragraph 7.19). We found that the Department used sound assumptions to project the costs of the transfer program and measure its sustainability. For example, the Department gave particular attention to assessing future growth in health care costs. The Minister of Finance was advised of the pros and cons of different CHT options and their associated long-term financial impact on governments, including the provinces and territories.

7.34 We conducted our own analyses and projections, based on the economic and fiscal conditions noted in the government's 2011 Update of Economic and Fiscal Projections. Assuming that the CHT growth rate remains at 6 per cent beyond 2013–14, we found that the new CHT measure should significantly improve the federal government's fiscal sustainability in the long run. Compared to a status quo scenario, the change in the rate of growth of the CHT could improve the federal debt-to-GDP ratio by almost 30 percentage points over a 40-year period.

7.35 Old Age Security. The Old Age Security program provides a monthly payment available to qualifying Canadians aged 65 and older. The Guaranteed Income Supplement (GIS) and spousal allowance provide additional support to low-income seniors, on top of the OAS payments. The 2012 Budget announced that the age of eligibility for OAS and GIS benefits would gradually increase from 65 to 67 over a

six-year period, starting in April 2023, with full implementation by January 2029. When it announced this change, the government did not release the cost savings or the overall long-term fiscal impact. Only academics and organizations have issued analyses on the sustainability of the program.

7.36 In 2009, at the request of the Department, a consultant produced a report comparing the pension systems of Canada and selected other OECD member countries. The report stated that there was “no pressing financial or fiscal need to increase pension ages in the foreseeable future.” However, it added, “The reduced benefit expenditures from a higher pension age could be used to augment the value of benefits, for example.” The report concluded that Canada’s retirement income system is strong compared to that of other countries. Nevertheless, the government announced changes to the age of OAS eligibility. In providing advice to the government, the Department considered a number of factors, including Canada’s shifting demographics, projected changes in the labour market, and the costs of the OAS program, in addition to international trends in the age of eligibility for public pension programs.

7.37 We examined whether the Department had estimated the long-term fiscal impact of the proposed changes. We found that the Department performed and considered a number of analyses to formulate recommendations on OAS. It estimated gross and net savings of raising the eligibility age from 65 to 67, and it included this information when it prepared a policy analysis on the measure. It also analyzed the measure’s impact on the provinces and territories. As well, the Department considered the impact on working Canadians and on labour force participation.

7.38 Analyses by the Department showed that the OAS program was one of the factors that could cause a deterioration in budgetary balances in the long term because annual average OAS spending is growing faster than the nominal GDP. One analysis concluded that potential OAS changes could help protect the fiscal sustainability of the federal government and create room for other spending priorities. In addition, according to the analysis, increasing the age of eligibility could improve labour market participation for older Canadians and provide some fiscal flexibility to deal with population aging. To assess how changing the OAS program would provide fiscal flexibility for the federal government over the next 40 years, the analyses considered scenarios with less favourable economic and fiscal assumptions, such as lower economic growth and lower tax revenues.

7.39 We performed an analysis replicating the economic and fiscal conditions found in the 2012 Budget. We found that without the announced OAS policy change, the expenses related to benefits for seniors would have risen from \$35.6 billion (2.2% of GDP) in the 2010–11 fiscal year to just over \$100 billion (2.9% of GDP) in 2029–30. The higher age of eligibility could reduce government expenses by over \$10 billion in 2029, when the government will have fully implemented the new policy.

7.40 In summary. We found that the Department considered analyses of long-term fiscal sustainability to be relevant for three of the measures we selected for review: the Tax-Free Savings Account, the new growth rate of the Canada Health Transfer, and the increase in the age of eligibility for Old Age Security benefits (Exhibit 7.3). Specifically, we found the following:

- The Department conducted the analyses and used them in formulating policy options.
- It prepared projections of long-term budgetary balance and public debt for the new CHT regime and the new age of eligibility for OAS.
- The TFSA analysis considered the impact on revenues, but it did not project the impact on the budgetary balance and public debt.
- For the three initiatives, the analyses took into account the fiscal impact on the provinces.

7.41 To determine the need for long-term fiscal analyses, departmental officials currently use their professional judgment, sometimes with discussions and input from senior management. In our view, relying on judgment to make the determination is a good approach, and detailed procedures may not be cost-effective. However, to ensure due diligence, it would be prudent to enhance existing practices for deciding on the need for long-term fiscal sustainability analyses. Better practices would also help the Department ensure that it gives adequate consideration to the long-term impact of measures on budgetary balance and public debt. For example, one such practice by which the long-term fiscal impact of policy recommendations might be better considered could be in preparing the briefing documents presented to the Minister of Finance. When seeking approval for policies or spending initiatives to be included in the Budget, the Department of Finance Canada officials use a template for preparing briefing documents for the Minister. This template could include long-term fiscal impacts of proposed policy initiatives.

Exhibit 7.3 The Department performed long-term fiscal sustainability analyses for some budget measures

| Measure | Analysis performed |
|---|--|
| 1) Pension income splitting | There was no analysis of the long-term fiscal impact. Officials assumed it was not relevant to consider the long-term cost because the growing proportion of families with two income earners would reduce the opportunity for income splitting. |
| 2) Reduction of the GST rate to 5% 3) Maintenance of the GST/HST credit as if the GST rate were 7% | Analyses for these two measures were not considered relevant because their costs relative to GDP were not expected to grow. |
| 4) Tax-Free Savings Account | Officials analyzed the long-term fiscal impact on revenues and considered the findings when formulating recommendations. The impact on revenues in the provinces was considered. There was no analysis or reporting of the long-term impact on budgetary balance and public debt. |
| 5) Canada Health Transfer | Officials analyzed the long-term fiscal impact on expenditures, budgetary balance, and public debt, and considered the findings when formulating recommendations. They also considered the impact on provincial/territorial governments when recommending policy options. |
| 6) Increase in age of eligibility for OAS | Officials analyzed the long-term fiscal impact on expenditures and considered the findings to support the decision-making process. They also considered the impact on budgetary balance and public debt, as well as the impact on the provinces and territories to inform decisions. |

Performing and publishing long-term analyses

7.42 Long-term fiscal analyses are not meant to precisely predict the government's future fiscal position. Rather, such analyses are best estimates that may vary from actual results because of changing economic and fiscal circumstances. Nevertheless, for policy makers, parliamentarians, and the general public, they can provide insight into the fiscal future and significant information for consideration in debates on budget proposals.

7.43 In recent years, the International Monetary Fund (IMF) and the Organisation for Economic Co-operation and Development (OECD) have issued a number of best practices and guidance documents regarding long-term fiscal sustainability reports. According to the OECD, governments should prepare yearly fiscal projections that include all public revenues and expenditures to support fiscal

stability and efficient resource allocation. In its Best Practices for Budget Transparency, the OECD recommends that projections cover a period of 10 to 40 years. Sound analyses on long-term fiscal sustainability need to rely on appropriate modelling techniques. They also need to use reasonable assumptions and sensitivity analyses to project the long-term impact of spending measures or policies. The OECD recommends that all key assumptions underlying the projections be made explicit.

7.44 We examined whether the Department of Finance Canada prepares and publishes projections on Canada's long-term fiscal position. We reviewed analyses of long-term fiscal sustainability produced by the Department. We also interviewed departmental officials and consulted with former officials and experts. Finally, using baseline projections derived from the 2012 Budget, we projected the federal government's overall long-term fiscal position to the 2050–51 fiscal year.

The Department prepares analyses of Canada's long-term fiscal position, but not in time to support budget decisions

7.45 We found that the Department of Finance Canada regularly prepared 10- and 40-year fiscal projections for the federal government. For example, it prepared budgetary balances and debt projections in August and November 2010, as well as in May, July, and November 2011. The projections described the overall fiscal position of the federal government in the long term. They contained analyses of the fiscal challenges presented by an aging population, including the fiscal impact of lower GDP growth, rising benefits for seniors, and increased health care spending. The projections took into account combined changes in revenues and expenses, considering the impact of known policy changes and evolving macroeconomic conditions. For example, in some recent analyses the Department concluded that if health care transfers grew faster than GDP, the long-term fiscal position of the federal government would become unsustainable. Since the Department considers the health care program an important national issue, the analyses also projected health care expenditures by province/territory and considered the impact of growing health care expenses on provincial/territorial budgets.

7.46 We found that the Department took the following actions for the economic and demographic assumptions it uses in making its projections:

- verified the assumptions for reasonableness,
- compared them with those of forecasters from the private sector and other organizations,

- included sensitivity analyses, and
- included analyses of different scenarios.

7.47 We found that fiscal sustainability analyses considered the long-term fiscal perspective for the provincial/territorial governments, as well as for the federal and provincial/territorial governments combined. For example, the Department prepared 45- and 55-year long-term fiscal projections for all provinces and territories combined, as well as for the provincial, territorial, and federal governments combined.

7.48 We found that senior management considered the results of the long-term fiscal analyses and regularly conveyed this information to the Minister of Finance. The Department prepared analyses after the fall economic and fiscal update, as well as after the tabling of the federal government's budget, but not before the budgetary process was concluded. Consequently, before the budget measures were approved, senior management and the Minister of Finance did not have access to long-term analyses describing the impact of those measures on the overall long-term fiscal position of the federal and provincial/territorial governments. For example, the Department officials told the audit team that the long-term projections that included the impact of the measures announced in the 2012 Budget were given to the Minister of Finance in August 2012. This means that senior management and the Minister of Finance were not informed of the overall impact of the 2012 Budget on the government's long-term fiscal position until well after they had approved budget measures.

7.49 Recommendation. As it concludes the budgetary process, the Department of Finance Canada should analyze the overall long-term fiscal implications for the federal government and should inform the Minister of Finance before budget measures are decided and approved.

The Department's response. Agreed. Starting with Budget 2013, the Department of Finance Canada will expand its internal analysis to provide the Minister of Finance with an assessment of the overall long-term fiscal implications of new budget measures before the budget is finalized.

The Department has not published analyses of Canada's long-term fiscal position

7.50 In its 2007 Budget, the federal government committed to publishing a comprehensive fiscal sustainability and intergenerational report. However, no such report has been published. The Department of Finance Canada last released information on the demographic challenge in an annex to the 2005 Budget; but except for health

spending, this did not contain long-term fiscal projections. A report drafted in 2007 included long-term fiscal projections for the federal and total government (federal, as well as provincial and territorial governments), but the government never published it. The Department has prepared other long-term fiscal sustainability analyses since 2010, but they too have not been made public.

7.51 Many OECD countries publish long-term fiscal projections (Exhibit 7.4). For example, Australia and New Zealand regularly publish 40-year projections. Norway, Switzerland, and the United Kingdom publish 50-year projections. The United States (through the Office of Management and Budget, the Congressional Budget Office, and the Government Accountability Office) publishes 75-year projections. Denmark, Sweden, the US and the UK report this information annually. The Netherlands publishes intergenerational accounts. In Canada, the Office of the Parliamentary Budget Officer has published a number of fiscal sustainability reports since 2010. Other than an ad hoc report in 2002, there has been no public reporting of long-term fiscal analyses by the Government of Canada.

7.52 There are significant benefits that would result from taking into account and publishing long-term projections of Canada's overall fiscal position. These benefits would include

- support for the decision-making process;
- better policy decisions that ensure intergenerational fairness, economic development, and the efficient use of public resources in the long term;
- enhanced long-term fiscal transparency to support policy and parliamentary debates;
- increased ability of Canadians to understand what our future might look like, based on a better assessment of whether budgets are fiscally prudent for the federal, provincial, and territorial governments;
- ability to hold leaders accountable for the long-term impact of their budget choices;
- greater ability of capital markets to anticipate the consequences of the government's long-term fiscal outlook;
- enhanced public sector credibility in the financial markets; and
- a demonstrated commitment on the part of the government to future budget sustainability.

Exhibit 7.4 Many Organisation for Economic Co-operation and Development countries publish reports on their long-term fiscal position

| Country | Statutory reporting obligations | Most recent report title (release date) | Time horizon | Periodically produced | Published comparison with past government assessments | Reported sensitivity analysis | Reported methodology and key assumptions | Published fiscal impact of past reforms or general policy options | Related to the budget |
|---|---|---|--------------|-----------------------------|---|-------------------------------|--|---|-----------------------|
| Australia | Charter of Budget Honesty Act 1998 | Intergenerational report 2010—Australia to 2050: future challenges (January 2010) | 40 years | Yes, every 3 years | Yes | Yes | Yes | No | Yes |
| Denmark | European Union (EU) Stability and Growth Pact | Convergence Programme Denmark 2012 (April 2012) | Until 2070 | Yes, annually | Yes | Yes | Yes | Yes | No |
| Germany | EU Stability and Growth Pact | Third Report on the Sustainability of Public Finances (October 2011) | Until 2060 | Yes, every 3 years | Yes | Yes | Yes | Yes | Yes |
| Korea | None | Vision 2030 (2006) | 25 years | No | No | No | No | No | No |
| Netherlands (Bureau for Economic Policy Analysis) | EU Stability and Growth Pact | Ageing Divided (June 2010) | Until 2200 | Yes, every 5 years | Yes | Yes | Yes | Yes | Yes |
| New Zealand | Public Finance Act 1989 | Challenges and Choices: New Zealand's Long-term Fiscal Statement (October 2009) | 40 years | Yes, at least every 4 years | Yes | Yes | Yes | Yes | Yes |
| Norway | None | Long-term Perspective for the Norwegian Economy (March 2009) | 50 years | Yes, at least every 4 years | No | No | Yes | Yes | Yes |
| Sweden | None | Spring Fiscal Policy Bill 2012 and Sweden's Convergence Programme 2012 | Until 2060 | Yes, annually | No | Yes | Yes | Yes | Yes |
| Switzerland | None | Long-term Sustainability of Public Finances in Switzerland (January 2012) | 50 years | Yes, at least every 4 years | No | Yes | Yes | No | Yes |

Exhibit 7.4 Many Organisation for Economic Co-operation and Development countries publish reports on their long-term fiscal position (continued)

| Country | Statutory reporting obligations | Most recent report title (release date) | Time horizon | Periodically produced | Published comparison with past government assessments | Reported sensitivity analysis | Reported methodology and key assumptions | Published fiscal impact of past reforms or general policy options | Related to the budget |
|---|--|---|--------------|-----------------------|---|-------------------------------|--|---|-----------------------|
| United Kingdom (Office for Budget Responsibility) | <i>Budget Responsibility and National Audit Act 2011</i> | Fiscal Sustainability Report (July 2012) | 50 years | Yes, annually | Yes | Yes | Yes | Yes | Yes |
| United States (Office of Management and Budget) | <i>Budget and Accounting Act of 1921</i> | Analytical Perspectives, Budget of the United States Government, Fiscal Year 2013 (February 2012) | 75 years | Yes, annually | Yes | Yes | Yes | Yes | Yes |
| United States (Department of the Treasury and Office of Management and Budget) | <i>Budget and Accounting Act of 1921</i> | 2011 Financial Report of the United States Government | 75 years | Yes, annually | No | Yes | No | No | No |
| United States (Congressional Budget Office) | No | The Long-Term Budget Outlook (June 2012) | 75 years | Yes, annually | Yes | No | Yes | Yes | Yes |
| United States (Government Accountability Office) | No | The Federal Government's Long-Term Fiscal Outlook—Fall 2011 Update | 75 years | Yes, annually | No | No | Yes | No | Yes |

Source: Adapted from the Organisation for Economic Co-operation and Development

7.53 We prepared fiscal projections to illustrate the impact of the 2012 Budget on the long-term fiscal sustainability of the federal government (Exhibit 7.5). The assumptions used in our long-term projections are generally consistent with those that the Department uses when projecting long-term fiscal balances and debt levels. Also, our long-term results are similar to the Department's projections. Our projections show that the combined measures announced in the budget significantly improved the government's fiscal outlook. These results are hypothetical since future policy decisions could take advantage of the projected surpluses to increase program benefits, introduce new spending initiatives, or reduce taxes.

Exhibit 7.5 The federal debt as a percentage of GDP is projected to decrease significantly over the long term as a result of measures from the 2012 Budget

Federal debt as a percentage of GDP



*Economic assumptions and economic conditions as in March 2012 Budget

Sensitivity analysis that shows the possible range of +/- 0.5 percent of nominal GDP

Note: This potential situation where the federal government starts accumulating wealth and has no more debt is hypothetical, since future policy decisions could take advantage of the projected fiscal dividends by increasing program benefits, introducing new spending initiatives, or reducing taxes.

7.54 According to our projections, in the 2050–51 fiscal year, the change to the Canada Health Transfer will account for about 60 percent of the government’s improved fiscal position, shown by the projected lower debt-to-GDP ratio. Our projections show that other policy decisions in the 2012 Budget will also contribute positively to the government’s long-term fiscal balance; examples are spending restraint measures and the change in the age of eligibility for seniors’ benefits. Even though the projections appear to be favourable, they must be interpreted carefully: they are estimates and are sensitive to changes in long-term assumptions and in future fiscal and economic conditions. Changes in factors such as GDP growth, interest rates, or productivity would affect the fiscal sustainability projections.

7.55 As shown in Exhibit 7.5, different GDP growth scenarios would shift the curve in the shaded area and make the government’s long-term fiscal position more or less favourable in the long term. In addition, future policy decisions could affect the government’s fiscal sustainability. In About the Audit, we included the assumptions we used to project the long-term debt-to-GDP ratios as well as analyses showing the impact and sensitivity of different assumptions and policy changes on the long-term projections.

7.56 We found that the Government of Canada has not followed through on its 2007 commitment to publish a long-term fiscal sustainability report. It is important to publish information on long-term fiscal sustainability analyses. In committing to publishing such analyses in 2007, the federal government held the view that maintaining sustainable public finances at all levels of government was a critical condition to achieving intergenerational equity and sustained economic growth. Although there are limitations in projecting 40 or 50 years into the future, an understanding of long-term fiscal trends is relevant when examining policy choices. The analyses of current and future demographic changes provide valuable information as well as the implication of these changes for Canada’s long-term economic and fiscal outlook overall. In this context, long-term fiscal sustainability analyses

- should include the long-term fiscal position of the federal government and the provinces and territories, as well as the position of the two levels of government combined to give a total Canada perspective;
- should be comprehensive and understandable to lay readers; and
- should be regularly reviewed and published because long-term projections are sensitive to changes in economic and fiscal conditions, in related assumptions, and in policy.

7.57 Recommendation. The Department of Finance Canada should publish yearly the overall long-term fiscal sustainability analyses for the federal government and provide from time to time an analysis for all governments combined, including the federal, provincial, and territorial governments, to give a total Canada perspective.

The Department's response. Agreed. Given that the federal government is not accountable for the fiscal situation of the provinces and territories, the Department will publish long-term fiscal analyses for the federal government on an annual basis, by 2013 at the latest.

Conclusion

7.58 Long-term fiscal projections and analyses are not meant to be precise. Nevertheless, they help raise fiscal sustainability issues for consideration during the budget process. They indicate whether spending and tax measures support fiscal sustainability in the long term, and whether these measures protect and improve the living standards of future generations. Sound fiscal projections can help minimize the risk that unaffordable fiscal pressures will force future governments to make sudden policy shifts.

7.59 We concluded that the Department of Finance Canada analyzed and informed the Minister of Finance about the long-term fiscal impact of budget measures. We found that the Department has the tools and capacity to prepare long-term fiscal sustainability analyses when considering spending or tax measures. But, we found that the Department analyzed long-term fiscal sustainability issues only when officials considered such analysis to be relevant. Senior officials used their judgment to determine the need for long-term fiscal analyses. Although there are opportunities for improvement, we concluded that the Department's approach is reasonable. For three of the six initiatives we reviewed, the Department analyzed the long-term impact on revenues or expenditures. For two of the three initiatives, the Department conducted long-term budgetary balance and public debt analyses. For all three initiatives, the Department considered the fiscal impact on the provinces. The Department considered the analyses that it performed when formulating recommendations.

7.60 We found that since 2010 the Department of Finance Canada regularly prepared sound long-term fiscal projections of the budgetary balance and public debt for the federal government. These projections captured the fiscal challenges of Canada's aging population. The Department reviewed the assumptions on which the projections were

based and made sure that they were reasonable. In addition, the projections took into account the impact on the provinces and territories. However, before the budget process was completed, the Department did not prepare projections of the impact that budgets would have on the fiscal position of the federal, provincial, and territorial governments. That is, it did not prepare the projections in time to influence or support budget decisions.

7.61 Finally, we found that the Government of Canada has not followed through on its 2007 commitment to publish a long-term fiscal sustainability report. Many member countries of the Organisation for Economic Co-operation and Development regularly publish such reports. Publicly available information on long-term fiscal sustainability would help policy makers, parliamentarians, and Canadians understand the long-term trajectory of the fiscal position of the federal, provincial, and territorial governments. It would also help them determine whether budgets are fiscally prudent, and would make leaders accountable for the long-term consequences of budget choices.

About the Audit

All of the audit work in this chapter was conducted in accordance with the standards for assurance engagements set by The Canadian Institute of Chartered Accountants. While the Office adopts these standards as the minimum requirement for our audits, we also draw upon the standards and practices of other disciplines.

Objectives

The audit examined whether the Department of Finance Canada considered the long-term fiscal impact in proposing measures and policies, as well as whether it publicly reported information related to long-term fiscal sustainability for Canada. The audit had the following sub-objectives:

- to determine whether the Department of Finance Canada analyzed long-term fiscal sustainability issues and informed decision makers of their results, and
- to determine whether the Department of Finance Canada prepared and published sound long-term fiscal sustainability analyses.

Scope and approach

The audit focused on the Department of Finance Canada, where we looked at the Economic and Fiscal Policy Branch.

The audit examined the process used by the Department for estimating the long-term fiscal impact when its officials consider spending and tax initiatives, and how the policy- and decision-making process takes into account this impact. As well, we looked at the process used by the Department to analyze long-term fiscal sustainability and publish reports.

We reviewed various documents, including briefing notes and analyses prepared by the Department as well as analyses, research papers, and foreign reports, including guidance issued by international organizations. We reviewed literature related to the issue of long-term fiscal sustainability. In addition, we consulted with former officials and experts in the field. We examined the analyses carried out by the Department of Finance Canada from 1 April 2006 to 31 March 2012. We did not examine how the fiscal impact of climate change or aging infrastructure is taken into account in the decision-making process at the Department. We examined practices for reporting information on long-term fiscal sustainability.

Assumptions used to project the long-term fiscal position of the federal government

The long-term economic and fiscal projections we developed are based on the projections contained in the applicable budget or economic and fiscal update. The assumptions used in our long-term projections are generally consistent with those that the Department uses.

Economic projections. The base projections for nominal gross domestic product (GDP) were taken from the applicable budget or economic and fiscal update. In each case, the long-term projections of nominal GDP growth are based on Statistics Canada's middle-growth population scenario, productivity growth of

about 1 percent per year, and inflation of 2 percent per year (consistent with the Bank of Canada's mid-point inflation target).

Fiscal projections. The long-term projections by major component after the reference period of the budget or economic and fiscal update were derived as shown in the following table.

| Projection | Method |
|---|--|
| Personal income taxes | The ratio of personal income tax to GDP for the final year of the applicable budget or economic and fiscal statement update was applied to the forecast of nominal GDP. To reflect the impact of the progressivity of the personal income tax system, the ratio increased by 0.02 per year. |
| Corporate income taxes and other income taxes | Based on growth in nominal GDP |
| Goods and services tax | Based on growth in nominal GDP |
| Customs import duties | Based on growth in nominal GDP |
| Other excise taxes and duties | Annual growth of 1.5% per year |
| Employment Insurance (EI) premium revenues | EI premium revenues are to be set to cover EI benefits and administration costs. The EI Operating Account should have no impact on the fiscal balance over time, although it could have a significant impact on an annual basis. For the purposes of this exercise, it is assumed that EI premium revenues would cover EI benefits and administration costs on an annual basis. |
| Other revenues | This is a highly volatile component, affected by exchange fund profits, offshore revenues, profits of Crown corporations (including the Bank of Canada), and interest payments on sovereign, student, and selected Crown corporation debt. Offshore revenue should have no impact on the budgetary balance as it is transferred to the applicable provinces and territories (with at the most a year's delay). Exchange Fund profits are too volatile to forecast, and so we have assumed no change. Revenues of Consolidated Crown corporations, share of annual profits by enterprise Crown corporations, sales of goods and services, and other miscellaneous revenues are extrapolated on the basis of change in population and inflation. Interest from enterprise Crown corporations, and interest and penalties, have been extrapolated based on a forecast of short-term interest rates. |
| Benefits for seniors | For the base case, current projections of Old Age Security program beneficiaries and expenditures from the Office of the Chief Actuary were linked to the final year of the 2012 Budget. |
| Employment Insurance benefits | We projected unemployment using the current relationship between the number of unemployed persons and the total population. Benefits are based on growth in the number of unemployed and inflation (benefits are indexed to changes in the average industrial wage). |
| Children's benefits | Based on the most current forecast of Statistics Canada (mid-case population projections) for the age group 0 to 14, and on inflation. |
| Transfers to other levels of government | Based on legislative parameters of the individual components: Canada Health Transfer (6% escalator until the 2016–17 fiscal year, followed by three-year moving average of nominal GDP growth thereafter), Canada Social Transfer (3% escalator), fiscal arrangements linked to growth in nominal GDP, Quebec Abatement linked to growth in nominal GDP, and Gas Tax Transfer held constant at \$2 billion per year. |
| Direct program expenses | Linked to growth in nominal GDP |
| Public debt charges | We broke down interest-bearing debt into short-term market debt, long-term market debt, the Public Service Pension Plan, and other future benefits. Public debt charges for the market debt were calculated using interest rates based on the applicable budget's or economic and fiscal update's short- and long-term interest rate forecasts. When surpluses are accumulated, the return on financial assets is assumed to be 3%. The interest rate used for interest expenses on the Public Service Pension Plan and other future benefits was 6%. |

The table below shows the impact of different assumptions for the projected federal debt-to-GDP ratio on the post-2012 Budget.

Sensitivity of post-2012 Budget projections

| Assumptions | Federal debt to GDP | | | | |
|--|---------------------|---------|---------|---------|---------|
| | 2017–18 | 2020–21 | 2030–31 | 2040–41 | 2050–51 |
| Base case | 27.2 | 23.5 | 10.1 | -6.8 | -26.8 |
| GDP growth (-0.1 p.p.*) | 27.2 | 23.7 | 10.6 | -5.7 | -25.4 |
| GDP growth (+0.1 p.p.) | 27.2 | 23.4 | 9.5 | -7.8 | -28.1 |
| Change in interest rate (-1 p.p.) | 26.9 | 22.5 | 7.2 | -9.8 | -28.0 |
| Change in interest rate (+1 p.p.) | 27.5 | 24.6 | 13.4 | -2.4 | -23.8 |
| Productivity (-0.3 p.p.) | 27.3 | 23.9 | 11.7 | -3.5 | -22.3 |
| Productivity (+0.3 p.p.) | 27.1 | 23.2 | 8.5 | -9.6 | -30.6 |
| 2016–17 personal income tax revenues (-\$10 billion) | 27.2 | 23.6 | 10.3 | -6.4 | -26.4 |
| 2016–17 personal income tax revenues (+\$10 billion) | 27.2 | 23.5 | 9.8 | -7.1 | -27.1 |
| 2016–17 direct program spending (-\$10 billion) | 26.7 | 21.6 | 2.9 | -18.7 | -42.5 |
| 2016–17 direct program spending (+\$10 billion) | 27.7 | 25.5 | 17.2 | 6.0 | -10.0 |

*p.p.: full percentage point

Criteria

| Criteria | Sources |
|--|--|
| To determine whether the Department of Finance Canada analyzed long-term fiscal sustainability issues and informed decision makers of the results, we used the following criteria: | |
| The Department of Finance Canada prepares sound analyses on long-term fiscal sustainability prior to recommending decisions regarding new (or changes to existing) policies and spending/tax measures. | <ul style="list-style-type: none"> Guidelines for Public Expenditure Management, International Monetary Fund Supplementary Document to the Department's 2011–12 Report on Plans and Priorities (RPP) Regarding Sustainable Development, Finance Canada OECD Best Practices for Budget Transparency, Organisation for Economic Co-operation and Development (OECD) The Benefits of Long-term Fiscal Projections, Organisation for Economic Co-operation and Development |
| To determine whether the Department of Finance Canada prepared and published sound long-term fiscal sustainability analyses, we used the following criteria: | |
| The Department of Finance Canada prepares sound analyses on Canada's long-term fiscal sustainability. | <ul style="list-style-type: none"> Code of Good Practices on Fiscal Transparency, International Monetary Fund, 2007 Budget 2007, Finance Canada The Benefits of Long-term Fiscal Projections, Organisation for Economic Co-operation and Development OECD Best Practices for Budget Transparency, Organisation for Economic Co-operation and Development |
| The Department of Finance Canada publishes comprehensive long-term fiscal sustainability information for Canada. | |

Management reviewed and accepted the suitability of the criteria used in the audit.

Period covered by the audit

The audit covered the period between April 2006 and March 2012. Audit work for this chapter was completed on 28 August 2012.

Audit team

Assistant Auditor General: Nancy Cheng

Principal: Richard Domingue

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For information, please contact Communications at 613-995-3708 or 1-888-761-5953 (toll-free).

Appendix List of recommendations

The following is a list of recommendations found in Chapter 7. The number in front of the recommendation indicates the paragraph where it appears in the chapter. The numbers in parentheses indicate the paragraphs where the topic is discussed.

| Recommendation | Response |
|---|--|
| Performing and publishing long-term analyses | |
| <p>7.49 As it concludes the budgetary process, the Department of Finance Canada should analyze the overall long-term fiscal implications for the federal government and should inform the Minister of Finance before budget measures are decided and approved. (7.45–7.48)</p> | <p>Agreed. Starting with Budget 2013, the Department of Finance Canada will expand its internal analysis to provide the Minister of Finance with an assessment of the overall long-term fiscal implications of new budget measures before the budget is finalized.</p> |
| <p>7.57 The Department of Finance Canada should publish yearly the overall long-term fiscal sustainability analyses for the federal government and provide from time to time an analysis for all governments combined, including the federal, provincial, and territorial governments, to give a total Canada perspective. (7.50–7.56)</p> | <p>Agreed. Given that the federal government is not accountable for the fiscal situation of the provinces and territories, the Department will publish long-term fiscal analyses for the federal government on an annual basis, by 2013 at the latest.</p> |

Report of the Auditor General of Canada to the House of Commons

Matters of Special Importance

Main Points—Chapters 1 to 7

Appendices

Planning the Use of Professional Service Contractors

Grant and Contribution Program Reforms

Protecting Canadian Critical Infrastructure Against Cyber Threats

Transition of Ill and Injured Military Personnel to Civilian Life

Real Property—National Defence

Transfer Payments to the Aerospace Sector—Industry Canada

Long-Term Fiscal Sustainability—Finance Canada



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**Matters of Special Importance
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Appendices**



Office of the Auditor General of Canada



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Office of the Auditor General of Canada

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Auditor General of Canada
Vérificateur général du Canada

To the Honourable Speaker of the House of Commons:

I have the honour to transmit herewith this 2012 annual Report to the House of Commons, which is to be laid before the House in accordance with the provisions of subsection 7(3) of the *Auditor General Act*.

Yours sincerely,

Michael Ferguson, FCA

OTTAWA, 23 October 2012



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Matters of Special Importance

Matters of Special Importance



Michael Ferguson, FCA
Auditor General of Canada

I am pleased to present my 2012 Fall Report to Parliament. The Report covers a range of activities that, together, represent billions of dollars entrusted to the federal government by the taxpayers of Canada.

Federal activities we examined include

- planning the use of professional service contractors,
- reforming grant and contribution programs,
- protecting critical infrastructure against cyber threats,
- supporting the transition of ill and injured military personnel to civilian life,
- managing National Defence's real property,
- supporting the aerospace sector through transfer payments, and
- working to achieve long-term fiscal sustainability.

Planning the Use of Professional Service Contractors

The federal government has identified an increasing need for a more flexible workforce, making this a good time to examine its strategic planning and assessment of contractor use. Current spending constraints underscore the need to ensure the best mix of resources to manage public funds in the most cost-effective manner.

The government spent \$8.1 billion in the 2010–11 fiscal year on professional and special services contracts with external individuals and organizations. We examined how Public Works and Government Services Canada, Health Canada, and Human Resources and Skills Development Canada plan their use of professional service contractors to supplement the knowledge and skills of public servants. Together, these departments reported that they spent just over \$2 billion on professional and special services contracts in 2010–11.

Grant and Contribution Program Reforms

The government transferred \$37 billion to individuals and organizations in the 2010–11 fiscal year through grant and contribution agreements. Properly planned and managed, grant and contribution programs provide an efficient means for the government to meet its policy objectives by enabling recipients to carry out activities that contribute to those objectives.

In response to a blue ribbon panel report, the government announced an action plan in May 2008 to reform the administration of grant and contribution programs by streamlining the administrative and reporting burden on recipients. Our audit examined whether the government has adequately implemented its action plan to date.

Protecting Canadian Critical Infrastructure Against Cyber Threats

Canada's critical infrastructure includes the computer-based systems that help run, for example, energy distribution networks, telecommunications networks, banking and manufacturing systems, as well as the government's own information systems. Cyber threats and electronic attacks through the Internet have been increasing in frequency and severity, and the federal government is concerned that the cyber threat environment is evolving more quickly than its ability to keep pace.

We examined whether selected federal departments and agencies are working with the provinces and territories and the private sector to protect critical Canadian infrastructure against cyber threats. This included looking at responsibilities for securing key government information systems.

Transition of Ill and Injured Military Personnel to Civilian Life

From 2006 to 2011, over 8,000 Canadian Forces members were released from the military because of an injury or illness that ended their military careers. Ill and injured members and veterans of the Canadian Forces have access to a variety of services, programs, and financial benefits to support their transition to civilian life.

Our audit examined how these services and benefits, estimated to cost about \$500 million in the 2010–11 fiscal year, are managed by National Defence and the Canadian Forces along with Veterans Affairs Canada.

Real Property—National Defence

Real property infrastructure is essential to the Canadian Forces' ability to carry out core missions in Canada and abroad. National Defence real property includes lands, some 20,000 buildings, and over 13,000 works such as roads, airfields, docks, and firing ranges. The Government's 2008 *Canada First* Defence Strategy commits to spending \$40 billion over 20 years, or 8 percent of all defence spending, on maintaining and renewing the Department's real property.

In 2010, National Defence reported a steady decline of the condition of its real property infrastructure since the 1990s. According to the Department, 43 percent of its non-residential buildings and 6 percent of works are over 50 years old. Our audit looked at how the Department is managing its real property at 21 main bases where Canadian Forces are organized, trained, equipped, and from which they are rapidly deployed.

Transfer Payments to the Aerospace Sector—Industry Canada

The federal government regards the aerospace sector as crucial to Canada's economic development, sovereignty, national security, and public safety. Since 2007, Industry Canada has authorized almost \$1.2 billion in assistance to the aerospace sector through two programs: the Strategic Aerospace and Defence Initiative (SADI), the federal government's second largest program of direct spending on research and development; and the Bombardier CSeries Program, intended to encourage research and development that will result in new commercial aircraft technologies.

We examined whether Industry Canada has enough information to assess the success of these programs. We also looked at whether the programs are managed according to the Treasury Board's Policy on Transfer Payments.

Long-Term Fiscal Sustainability—Finance Canada

Long-term fiscal sustainability refers to a government's capacity to finance its activities and debt obligations in the future without imposing an unfair burden on future generations. In 2011, the Office of the Auditor General encouraged the government to publish the long-term financial projections needed to fully assess the impact of the challenges facing the country and to inform Canadians.

In this audit, we examined whether the Department of Finance Canada takes into account the impact of spending and tax measures on long-term fiscal sustainability before recommending new policies. We also examined how analyses of long-term fiscal sustainability are prepared and reported.

Conclusion

I trust that parliamentarians will find the information in this report useful in holding government to account for its management of resources.

Main Points—Chapters 1 to 7

Planning the Use of Professional Service Contractors

Chapter 1 Main Points

| What we examined | The need for human resources in organizations can be met by hiring additional staff or through contracting. In the federal government, professional service contractors can be engaged to meet unanticipated changes in workload and to obtain specialized expertise. This resourcing option provides managers with the necessary flexibility to meet their operational needs or to obtain expertise that is not available in a department or agency. |
|--------------------|--|
| | Professional services are usually provided by self-employed individuals or independent organizations engaged for a fixed period of time to provide expertise in such areas as information technology, management consulting, health services, and engineering and architecture. The specific conditions and details of the work to be performed are outlined in a contract. |
| | We audited Public Works and Government Services Canada, Health Canada, and Human Resources and Skills Development Canada. Together, these departments reported that they spent just over \$2 billion on professional and special services contracts in the 2010–11 fiscal year, about 25 percent of the total amount spent government-wide on contracts in this category. We examined whether these three departments adequately plan their use of professional service contractors. We did not audit how contracts were administered and amended. |
| | Audit work for this chapter was completed on 17 July 2012. Details on the conduct of the audit are provided in About the Audit at the end of the chapter. |
| Why it's important | The federal government spent \$8.1 billion in the 2010–11 fiscal year on professional and special services contracts with external individuals and organizations. When used strategically, professional service contractors complement the existing workforce by supplementing the knowledge and skills of public servants. Several recent audits and studies in Canada and other countries have recognized the need to strategically |

manage contracted professional services, and have also raised concerns about contractors being used to complement the work of public servants on a long-term basis.

In the current environment of fiscal restraint, departments and agencies have been under pressure to reduce their expenditures and increase the flexibility of their workforce. At the same time, they need to carefully plan their use of contractors to ensure that they mitigate potential risks such as loss of corporate knowledge and in-house expertise.

What we found

- The three departments we examined plan for their need for employees and contractors separately. That is, they do not consider employee and contracting information together when making resourcing decisions. This hampers the ability of these departments to consider the full range of resourcing options available to them. As such, these departments may not be able to reassess whether the mix of employees and contractors is still optimal to achieve their business objectives. Public Works and Government Services Canada has begun to change its resource planning processes for the 2012–13 fiscal year, with a view to integrating human resource planning with other planning processes.
- Health Canada and Human Resources and Skills Development Canada primarily plan for contractor use at the project and program levels. This reduces their ability to collect or analyze information at a high enough level to fully assess departmental needs and to identify ongoing resource gaps. These two departments also conduct limited assessment of the benefits, costs, and risks of contractor use at the branch or department level.

The departments have responded. The departments agree with our recommendations. Their detailed responses follow the recommendations throughout the chapter.

Grant and Contribution Program Reforms

Chapter 2

Main Points

What we examined

The federal government transfers money to individuals and to organizations of various types, including businesses and other governments. In 2010–11, transfer payments totalled \$158 billion. The majority of those payments—\$121 billion—were transferred to other levels of government and individuals through programs with ongoing spending authority. However, a significant portion—\$37 billion—was transferred through grant and contribution agreements. Our audit focused on grant and contribution programs.

Our last audit that focused specifically on grants and contributions was in 2006, after which an independent Blue Ribbon Panel commissioned by the President of the Treasury Board of Canada recommended that the government streamline the administrative and reporting burden on grant and contribution recipients. In May 2008, the government announced an action plan to reform the administration of grant and contribution programs.

In this audit, we examined whether the government has adequately implemented its action plan to date. We focused on the role played by the Treasury Board of Canada Secretariat (the Secretariat) in leading the reforms. We also examined selected activities undertaken in five federal organizations to implement the reforms.

Audit work for this chapter was completed on 17 July 2012. More details on the conduct of the audit are in **About the Audit** at the end of this chapter.

Why it's important

Properly planned and managed, grant and contribution programs provide an efficient means for the government to meet its policy objectives. Grants and contributions enable recipients to carry out activities that contribute to the government's objectives.

In its 2006 report, the independent Blue Ribbon Panel on Grants and Contributions concluded that fundamental change was needed to make the delivery of grants and contributions more efficient. It said that simplifying administration while strengthening accountability was both possible and necessary, and would require sustained leadership.

What we found

- To date, the federal government has adequately implemented the 2008 Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs, which is aimed at increasing efficiencies and reducing the administrative burden on recipients. However, neither the Treasury Board of Canada Secretariat nor the five organizations we examined have assessed the full impact of implementing the Government Action Plan on either their own administrative processes or the administrative burden on the recipients of their programs. Therefore, they cannot determine how much, if at all, their actions have led to streamlined administrative processes within federal organizations or a reduced administrative burden on recipients.
- The Treasury Board of Canada Secretariat actively led the implementation of the Government of Canada Action Plan to Reform the Administration of Grant and Contribution Programs. It led efforts to develop and obtained Treasury Board approval for a new Policy on Transfer Payments. The Secretariat also provided leadership and guidance to federal organizations to make the necessary changes, including coordinating activities across the government.
- The federal organizations we examined have taken action on most of their obligations under the new Policy on Transfer Payments. They have consulted with their applicant and recipient communities in re-designing their grant and contribution programs, and have begun to establish service standards.
- The organizations we examined have conducted risk assessments of their programs and their recipient communities and have assigned a risk rating to each recipient based on the assessments. However, despite the importance of these ratings in determining the controls that should be applied in each case—such as the extent of monitoring and reporting required—the Treasury Board of Canada Secretariat has not provided organizations with adequate guidance to ensure that risk ratings are accurate and remain current.

The Secretariat has responded. The Treasury Board of Canada Secretariat agrees with all of the recommendations. Its detailed responses follow the recommendations throughout the chapter.

Protecting Canadian Critical Infrastructure Against Cyber Threats

Chapter 3

Main Points

What we examined

Critical infrastructure consists of physical and information technology assets, such as the electricity distribution networks, telecommunications networks, banking systems, manufacturing and transportation systems, as well as government information systems and services that support the continued and effective functioning of government. Elements of critical infrastructure can be stand-alone or interconnected and interdependent within and across provinces, territories, and international borders. Most of Canada's critical infrastructure is owned by the private sector or by municipal, provincial, or territorial governments, and much of it is connected to other systems.

Cyber threats to Canada's critical infrastructure refer to the risk of an electronic attack through the Internet. Such attacks can result in the unauthorized use, interruption, or destruction of electronic information or of the electronic and physical infrastructure used to process, communicate, or store that information.

Our audit examined whether selected federal departments and agencies are working with the provinces and territories and the private sector to protect Canada's critical infrastructure against cyber threats. This included examining leadership roles and responsibilities for securing key government information systems.

Audit work for this chapter was completed on 17 July 2012. More details on the conduct of the audit are in **About the Audit** at the end of this chapter.

Why it's important

Canada's public and private sectors depend on a secure, robust, and stable information infrastructure to conduct day-to-day operations. Computer-based systems, together with their Internet and network connections, form the backbone for much of Canada's critical infrastructure, including the energy, finance, telecommunications, and manufacturing sectors as well as government information systems. The smooth operation of critical infrastructure supports our way of life and Canada's economic, political, and social well-being.

Attacks on aspects of critical infrastructure of many nations, including Canada, have been reported. The government has stated that the frequency and severity of cyber threats are accelerating and it considers that protecting Canadians in cyberspace will be a constantly evolving challenge. The government has concerns that the cyber threat environment is evolving more rapidly than the government's ability to keep pace.

What we found

- Between 2001 and 2009, the government made limited progress in its efforts to lead and coordinate the protection of Canada's critical infrastructure from cyber threats as these threats were rapidly evolving. During this time, the government released several strategies and policies with recurring commitments and funding.
- Since 2010, with the announcement of the Cyber Security Strategy and of the National strategy and action plan for critical infrastructure, the government has made progress in securing its systems against cyber threats, in improving communications, and in building partnerships with owners and operators of critical infrastructure.
- Eleven years after the government said it would establish partnerships with other levels of government and with critical infrastructure owners and operators to help protect Canada's critical infrastructure, not all of the sector networks that facilitate these partnerships are fully established, and coverage is incomplete. This lack of progress limits Public Safety Canada's ability to communicate with critical infrastructure owners and operators.
- Seven years after the Canadian Cyber Incident Response Centre (CCIRC) was created to collect, analyze, and share cyber threat information among federal departments, provincial and territorial governments, and the private sector, many stakeholders are still unclear about the Centre's role and mandate. As a result, the CCIRC cannot fully monitor Canada's cyber threat environment, which hinders the Centre's ability to provide timely advice on defending against new cyber threats. Furthermore, the Centre is still not operating on a 24-hour-a-day, 7-day-a-week basis, as originally intended. This restriction on operating hours can delay the detection of emerging threats and the sharing of related information among stakeholders.

- The January 2011 intrusion on government systems identified weaknesses in protecting these systems. Incidents were not reported in a timely manner and cyber threat information was not properly shared with appropriate agencies. Also, good information technology (IT) security practices, such as how to store sensitive information, were not consistently followed. Lead security agencies are taking action by updating the government's IT Incident Management Plan to clarify the roles and responsibilities of lead security agencies and to address the need for timely reporting of incidents. The government has allocated more funds to bolster its capacity to detect cyber threats, and is working to increase awareness of best practices for IT security across the government.

The entities have responded. The entities agree with all of the recommendations. Their detailed responses follow the recommendations throughout the chapter.

Transition of Ill and Injured Military Personnel to Civilian Life

Chapter 4

Main Points

What we examined

From 2006 to 2011, 8,026 Canadian Forces members were released from the military because of an injury or illness that ended their military career. Ill and injured members and veterans of the Canadian Forces have access to a variety of services, programs, and financial benefits to support their transition from military to civilian life.

Support services and benefits, including those available under the New Veterans Charter, are provided, coordinated, and managed primarily by the Department of National Defence and the Canadian Forces, and Veterans Affairs Canada.

Our audit looked at selected services and benefits provided to support eligible Canadian Forces members and veterans in their transition to civilian life. We examined how the Department of National Defence and the Canadian Forces, and Veterans Affairs Canada manage those services and benefits.

We did not look at whether Canadian Forces members and veterans have received all benefits and services for which they were eligible. Neither did we examine the fairness of departmental services and benefits available, or the quality of medical treatment and care provided.

Audit work for this chapter was completed on 17 July 2012. More details on the conduct of the audit are in **About the Audit** at the end of the chapter.

Why it's important

Ill and injured members of the Canadian Forces and their families may need support in making the transition to civilian life and in coping with their illnesses and injuries. Others who have left the military may develop physical and/or mental health problems over time that are associated with their military service and become eligible for support. Research shows that early detection and appropriate treatment of illness and injuries can have a critical impact on the success of this support, which amounted to about \$500 million in the 2010–11 fiscal year.

How well National Defence and the Canadian Forces, and Veterans Affairs Canada coordinate and manage this support affects the quality of the transition to civilian life that ill and injured Canadian Forces members and veterans are able to make.

What we found

- Canadian Forces members and veterans, as well as departmental staff responsible for assessing eligibility and managing the delivery of services and benefits, find the transition process complex, lengthy, and challenging to navigate. Although National Defence and the Canadian Forces, and Veterans Affairs Canada recognize the challenges and have been working independently and jointly on solutions, it remains difficult to access services and benefits in a timely manner. Reasons include the complexity of eligibility criteria, lack of clear information on support available, the amount of paperwork involved, and case management services that require further improvement.
- Both departments have difficulties in communicating and meeting service delivery standards and requirements, particularly as they relate to assessments and case management services. The result may be that Forces members and veterans do not receive benefits and services to which they are entitled, or do not receive them in a timely manner.
- An overarching governance framework has been established to coordinate, harmonize, and communicate the various programs, services, and benefits available to ill and injured Forces members and veterans. However, it does not specify the authority, responsibility, and accountability of the joint steering committee—the key coordinating mechanism meant to help manage the transition, reintegration, and continuity of support to Forces members and veterans. In addition, measurable objectives and specific timelines have not been established for all joint priorities approved by the committee. The existence of similar income support and vocational rehabilitation programs within each department continues to create confusion and difficulties for veterans and program staff alike.

The departments have responded. The departments agree with all of the recommendations. Their detailed responses follow the recommendations throughout the chapter.

Real Property—National Defence

Chapter 5 Main Points

What we examined

The Department of National Defence's real property includes lands, some 20,000 buildings, and over 13,000 works in installations and bases across Canada. Buildings can include armouries and barracks, storage and maintenance facilities, and hangars. Works are divided between service works such as roads, sewers, and fuel tanks, and operational works such as airfields, docks, and firing ranges. This infrastructure provides critical support to operations. It is used to sustain military personnel, provide training facilities, store and protect essential material, and deploy forces.

We examined whether National Defence has exercised sound stewardship in managing its real property. Audit work focused on the systems and practices used to deliver infrastructure at 21 main bases at which forces are organized, trained, and equipped and from which they are rapidly deployed. Residential housing was excluded from the scope of the audit.

Audit work for this chapter was completed on 17 July 2012. More details on the conduct of the audit are provided in **About the Audit** at the end of the chapter.

Why it's important

Real property infrastructure is essential to the Canadian Forces' ability to undertake core missions in Canada and abroad. It is one of four pillars of the Government's 2008 *Canada First* Defence Strategy to build an effective military. The strategy commits to spending \$40 billion over 20 years, or 8 percent of all defence spending, on maintaining and renewing the Department's real property.

National Defence reported in 2010 a steady decline of the condition of its real property infrastructure since the 1990s. According to the Department, 43 percent of its non-residential buildings and 61 percent of works were over 50 years old. Older infrastructure is typically less suited to serve current needs and, when not maintained in good condition, it carries increased risks of operational failure or risks to health and safety. Given the size, complexity, and extent of National Defence's portfolio and its critical impact on the Canadian Forces' operational capabilities, it is important that it be managed accordingly.

What we found

- National Defence has not yet put in place a real property management framework or national strategy for managing real property. Both have been drafted but neither has been approved and issued. The draft strategy lays out a roadmap to achieve stewardship, including a new portfolio management approach, stewardship reporting, integrated real property management, a new performance management and reporting framework, updated information systems, and risk-based investment planning. The framework requires master real property development plans at the bases and a national master real property development plan. Some of these elements are in place but until the strategy, framework, and a national master real property development plan are complete, the Department cannot know if it has the required real property assets at the right place, at the right time, to meet the operational requirements of the Canadian Forces.
- There are gaps in National Defence's management practices for acquiring, maintaining, and repairing capital assets. Headquarters have not provided bases with performance objectives and targets for important performance indicators such as indices of condition or suitability of real property. The overall performance management framework for real property is incomplete and headquarters do not have the information they need to assess the condition of real property assets. The Department's approval process for construction projects is cumbersome and lengthy. Planning and delivery of important projects takes about six years. Preventive maintenance practices are insufficient. The focus is often on maintenance after breakdown, resulting in a premature failure of real property assets. Many locations were found to not be compliant with the National Fire Code of Canada. For example, required inspections of fire alarms were often not being conducted. There were instances of non-compliance with other health and safety requirements. This means that the health and safety of workers in the affected facilities could be at risk.
- National Defence has been unable to meet its expenditure targets for maintenance and repair and recapitalization. Bases often do not receive funds for maintenance and repair and recapitalization early enough in the fiscal year to match plans and projects with the construction cycle. The Department reports that its inability to meet targets is due in part to a lack of personnel but it cannot expect significantly more human resources. National Defence will have to transform the way it manages real property to fulfill all the requirements of sound stewardship.

The Department has responded. National Defence agrees with all of the recommendations. Its detailed responses follow the recommendations throughout the chapter.

Transfer Payments to the Aerospace Sector—Industry Canada

Chapter 6

Main Points

What we examined

Since 2007, Industry Canada has authorized assistance of almost \$1.2 billion through two transfer payment programs to the aerospace sector: the Strategic Aerospace and Defence Initiative (SADI) and the Bombardier CSeries Program. SADI is the federal government's second largest program of direct spending on research and development, created to support private sector industrial research and pre-competitive development in Canada's aerospace, defence, security, and space industries through repayable project contributions. The Department has 25 individual SADI projects with recipients.

Industry Canada also manages two repayable contribution agreements for the Bombardier CSeries Program. These contributions are intended to encourage research and development that will result in the development of new commercial aircraft technologies.

We examined whether Industry Canada had sufficient information to determine if the transfer payments were meeting the programs' objectives. We also looked at whether the Department managed these programs according to the key requirements of the Treasury Board's Policy on Transfer Payments and the terms and conditions of the programs. In addition, we examined whether Industry Canada collected repayments from recipients for contributions that are repayable under two previous transfer payment programs: the Defence Industry Productivity Program and Technology Partnerships Canada.

Audit work for this chapter was completed on 17 July 2012. More details on the conduct of the audit are in **About the Audit** at the end of this chapter.

Why it's important

The federal government regards the aerospace sector as crucial to Canada's economic development, sovereignty, national security, and public safety. Aerospace companies are important contributors to the Canadian economy. National Research Council Canada reported that Canada's aerospace sector is the fifth largest in the world, as of 2008, with total aerospace sector revenues reaching \$23 billion.

What we found

- Before 2010, Industry Canada had inadequate performance information to determine progress being made to achieve the Strategic Aerospace and Defence Initiative's objectives. Since 2010, the Department has made improvements and now collects and consolidates sufficient information to allow it to determine progress against the program's objectives. However, the Department has not followed through on its commitments to report publicly on the program's results. As well, the Department will need to follow through on commitments to collect additional performance information so that it can complete its planned evaluation of the program in 2016–17. For the Bombardier CSeries Program, the Department has not collected all documents required by the contribution agreements to determine progress toward the program's objectives, so it has a more limited picture of the program's performance.
- Industry Canada has managed most aspects of these transfer payment programs appropriately, using a control framework that is reasonable—for example, it reviews recipients' claims and progress reports before issuing payments. As well, the Department funded only recipients that met program eligibility requirements. It also undertook a detailed review of proposed projects before signing contribution agreements with recipients. However, the Department did not define the appropriate level of monitoring and reporting for the different levels of risk assigned to the projects and for the amount of funding provided to individual recipients.
- In cases where contributions under the Defence Industry Productivity Program and Technology Partnerships Canada were repayable, the majority of repayments we examined were obtained by Industry Canada on time.

The Department has responded. The Department agrees with our recommendations. Its detailed responses follow the recommendations throughout the chapter.

Long-Term Fiscal Sustainability— Finance Canada

Chapter 7

Main Points

What we examined

Long-term fiscal sustainability refers to a government's capacity to finance its activities and debt obligations in the future without imposing an unfair burden on future generations.

In its 2007 Budget, the federal government committed to publishing a comprehensive fiscal sustainability and intergenerational report aimed at providing "a broad analysis of current and future demographic changes and the implication of these changes for Canada's long-run economic and fiscal outlook." In 2011, the Office of the Auditor General encouraged the government to publish the long-term financial projections needed to fully assess the impact of the challenges facing the country and to inform Canadians.

We examined whether the Department of Finance Canada takes into account the impact of spending and tax measures on long-term fiscal sustainability before recommending new policies. We also examined how analyses of long-term fiscal sustainability are prepared and reported.

Audit work for this chapter was completed on 28 August 2012. More details on the conduct of the audit are in [About the Audit](#) at the end of this chapter.

Why it's important

The government faces many ongoing challenges that could impact Canada's long-term fiscal sustainability, such as changing demographics, climate change, and aging infrastructure. If the public debt were to grow faster than the economy for a long period, these challenges could make public finances unsustainable and reduce the living standard of future generations.

Long-term fiscal projections can help governments understand and protect the sustainability of public finances and respond more effectively to financial pressures in the future. Though long-term projections of fiscal sustainability are not predictions, they underpin fiscal sustainability and inform fiscal policy decisions. Understanding and considering the possible future consequences of fiscal decisions support sound economic development and the efficient use of available resources.

What we found

- Finance Canada officials prepare long-term fiscal analyses of spending and tax measures only if they consider it relevant to do so. Therefore, if the fiscal impact of measures being considered is not expected to change significantly relative to the size of the economy, the Department will not project the impact beyond five years. Although there are opportunities for improvements, we concluded that this approach, where officials use their professional judgment to determine whether the long-term fiscal impact needs to be considered, is reasonable. When officials do consider it relevant to perform analyses, they assess the long-term impact of individual measures on revenues or expenditures but do not always assess the impact on the budgetary balance and the public debt. Nor do they always project how the measures support or hinder long-term fiscal sustainability. Departmental officials rely on sometimes incomplete analyses of the long-term impact of measures when formulating recommendations.
- Regularly since 2010 and on occasion before that, Finance Canada has been providing the Minister of Finance with the results of fiscal sustainability analyses that project budgetary balance and public debt in the long term. However, the Department does not prepare these analyses—which indicate how budget measures will impact the fiscal position of the federal, provincial, and territorial governments—in time to inform budget decisions and before budgets are tabled in Parliament. For a given budget, the Minister is not informed of the overall long-term fiscal impact until months after the budget measures have been approved.
- While Finance Canada prepared a draft report in 2007 on the long-term fiscal sustainability analyses that the government committed to issuing that year, the analyses were not published; nor has any report on long-term fiscal sustainability been published since then. While long-term fiscal sustainability analyses have been regularly prepared since 2010, they have not been made public. This lack of reporting means that parliamentarians and Canadians do not have all the relevant information to understand the long-term impact of budgets on the federal, provincial, and territorial governments in order to support public debate and to hold the government to account. Many of the countries that are members of the Organisation for Economic Co-operation and Development (OECD) already publish reports on their long-term fiscal positions.

The Department has responded. The Department agrees with all of the recommendations. Its detailed responses follow the recommendations throughout the chapter.

Appendices

Appendix A Auditor General Act

An Act respecting the office of the Auditor General of Canada and sustainable development monitoring and reporting

Short Title

- Short title** 1. This Act may be cited as the *Auditor General Act*.

Interpretation

- Definitions** 2. In this Act,
- “appropriate Minister”** “appropriate Minister” has the meaning assigned by section 2 of the *Financial Administration Act*;
- “Auditor General”** “Auditor General” means the Auditor General of Canada appointed pursuant to subsection 3(1);
- “category I department”** “category I department” means
 - (a) any department named in schedule I to the *Financial Administration Act*,
 - (b) any department in respect of which a direction has been made under subsection 11(3) of the *Federal Sustainable Development Act*; and
 - (c) any agency set out in the schedule to the *Federal Sustainable Development Act*.
- “Commissioner”** “Commissioner” means the Commissioner of the Environment and Sustainable Development appointed under subsection 15.1(1);
- “Crown corporation”** “Crown corporation” has the meaning assigned to that expression by section 83 of the *Financial Administration Act*;
- “department”** “department” has the meaning assigned to that term by section 2 of the *Financial Administration Act*;
- “funding agreement”** “funding agreement” has the meaning given to that expression by subsection 42(4) of the *Financial Administration Act*;
- “recipient”** “recipient” has the meaning given to that expression by subsection 42(4) of the *Financial Administration Act*;
- “registrar”** “registrar” means the Bank of Canada and a registrar appointed under Part IV of the *Financial Administration Act*;

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| “sustainable development” | “sustainable development” means development that meets the needs of the present without compromising the ability of future generations to meet their own needs; |
| Control | <p>2.1 (1) For the purpose of paragraph (d) of the definition “recipient” in subsection 42(4) of the <i>Financial Administration Act</i>, a municipality or government controls a corporation with share capital if</p> <ul style="list-style-type: none"> (a) shares of the corporation to which are attached more than fifty per cent of the votes that may be cast to elect directors of the corporation are held, otherwise than by way of security only, by, on behalf of or in trust for that municipality or government; and (b) the votes attached to those shares are sufficient, if exercised, to elect a majority of the directors of the corporation. |
| Control | <p>(2) For the purpose of paragraph (d) of the definition “recipient” in subsection 42(4) of the <i>Financial Administration Act</i>, a corporation without share capital is controlled by a municipality or government if it is able to appoint the majority of the directors of the corporation, whether or not it does so.</p> |
| Auditor General of Canada | |
| Appointment | <p>3. (1) The Governor in Council shall, by commission under the Great Seal, appoint an Auditor General of Canada after consultation with the leader of every recognized party in the Senate and House of Commons and approval of the appointment by resolution of the Senate and House of Commons.</p> |
| Tenure | <p>(1.1) The Auditor General holds office during good behaviour for a term of 10 years but may be removed for cause by the Governor in Council on address of the Senate and House of Commons.</p> |
| | <p>(2) [Repealed, 2011, c. 15, s. 17]</p> |
| Re-appointment | <p>(3) Once having served as the Auditor General, a person is not eligible for re-appointment to that office.</p> |
| Interim appointment | <p>(4) In the event of the absence or incapacity of the Auditor General or if that office is vacant, the Governor in Council may appoint any qualified auditor to hold that office in the interim for a term not exceeding six months, and that person shall, while holding office, be paid the salary or other remuneration and expenses that may be fixed by the Governor in Council.</p> |

- Salary**
4. (1) The Auditor General shall be paid a salary equal to the salary of a puisne judge of the Supreme Court of Canada.
- Pension benefits**
- (2) The provisions of the *Public Service Superannuation Act*, other than those relating to tenure of office, apply to the Auditor General except that a person appointed as Auditor General from outside the public service may, by notice in writing given to the President of the Treasury Board not more than sixty days after the date of his appointment as Auditor General, elect to participate in the pension plan provided for in the *Diplomatic Service (Special) Superannuation Act* in which case the provisions of that Act, other than those relating to tenure of office, apply to him and the provisions of the *Public Service Superannuation Act* do not apply to him.
- Powers and Duties**
- Examination**
5. The Auditor General is the auditor of the accounts of Canada, including those relating to the Consolidated Revenue Fund and as such shall make such examinations and inquiries as he considers necessary to enable him to report as required by this Act.
- Idem**
6. The Auditor General shall examine the several financial statements required by section 64 of the *Financial Administration Act* to be included in the Public Accounts, and any other statement that the President of the Treasury Board or the Minister of Finance may present for audit and shall express his opinion as to whether they present fairly information in accordance with stated accounting policies of the federal government and on a basis consistent with that of the preceding year together with any reservations he may have.
- Annual and additional reports to the House of Commons**
7. (1) The Auditor General shall report annually to the House of Commons and may make, in addition to any special report made under subsection 8(1) or 19(2) and the Commissioner's report under subsection 23(2), not more than three additional reports in any year to the House of Commons
- (a) on the work of his office; and,
- (b) on whether, in carrying on the work of his office, he received all the information and explanations he required.

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| Idem | <p>(2) Each report of the Auditor General under subsection (1) shall call attention to anything that he considers to be of significance and of a nature that should be brought to the attention of the House of Commons, including any cases in which he has observed that</p> <ul style="list-style-type: none"> (a) accounts have not been faithfully and properly maintained or public money has not been fully accounted for or paid, where so required by law, into the Consolidated Revenue Fund; (b) essential records have not been maintained or the rules and procedures applied have been insufficient to safeguard and control public property, to secure an effective check on the assessment, collection and proper allocation of the revenue and to ensure that expenditures have been made only as authorized; (c) money has been expended other than for purposes for which it was appropriated by Parliament; (d) money has been expended without due regard to economy or efficiency; (e) satisfactory procedures have not been established to measure and report the effectiveness of programs, where such procedures could appropriately and reasonably be implemented; or (f) money has been expended without due regard to the environmental effects of those expenditures in the context of sustainable development. |
| Submission of annual report to Speaker and tabling in the House of Commons | <p>(3) Each annual report by the Auditor General to the House of Commons shall be submitted to the Speaker of the House of Commons on or before December 31 in the year to which the report relates and the Speaker of the House of Commons shall lay each such report before the House of Commons forthwith after receiving it or, if that House is not then sitting, on any of the first fifteen days on which that House is sitting after the Speaker receives it.</p> |
| Notice of additional reports to Speaker and tabling in the House of Commons | <p>(4) Where the Auditor General proposes to make an additional report under subsection (1), the Auditor General shall send written notice to the Speaker of the House of Commons of the subject-matter of the proposed report.</p> |
| Submission of additional reports to Speaker and tabling in the House of Commons | <p>(5) Each additional report of the Auditor General to the House of Commons made under subsection (1) shall be submitted to the House of Commons on the expiration of thirty days after the notice is sent pursuant to subsection (4) or any longer period that is specified in the notice and the Speaker of the House of Commons shall lay each such report before the House of Commons forthwith after receiving it or, if that House is not then sitting, on any of the first fifteen days on which that House is sitting after the Speaker receives it.</p> |

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| Inquiry and report | <p>7.1 (1) The Auditor General may, with respect to a recipient under any funding agreement, inquire into whether</p> <ul style="list-style-type: none"> (a) the recipient has failed to fulfil its obligations under any funding agreement; (b) money the recipient has received under any funding agreement has been used without due regard to economy and efficiency; (c) the recipient has failed to establish satisfactory procedures to measure and report on the effectiveness of its activities in relation to the objectives for which it received funding under any funding agreement; (d) the recipient has failed to faithfully and properly maintain accounts and essential records in relation to any amount it has received under any funding agreement; or (e) money the recipient has received under any funding agreement has been expended without due regard to the environmental effects of those expenditures in the context of sustainable development. |
| Report | <p>(2) The Auditor General may set out his or her conclusions in respect of an inquiry into any matter referred to in subsection (1) in the annual report, or in any of the three additional reports, referred to in subsection 7(1). The Auditor General may also set out in that report anything emerging from the inquiry that he or she considers to be of significance and of a nature that should be brought to the attention of the House of Commons.</p> |
| Special report to the House of Commons | <p>8. (1) The Auditor General may make a special report to the House of Commons on any matter of pressing importance or urgency that, in the opinion of the Auditor General, should not be deferred until the presentation of the next report under subsection 7(1).</p> |
| Submission of reports to Speaker and tabling in the House of Commons | <p>(2) Each special report of the Auditor General to the House of Commons made under subsection (1) or 19(2) shall be submitted to the Speaker of the House of Commons and shall be laid before the House of Commons by the Speaker of the House of Commons forthwith after receipt thereof by him, or if that House is not then sitting, on the first day next thereafter that the House of Commons is sitting.</p> |

Idem

9. The Auditor General shall

- (a) make such examination of the accounts and records of each registrar as he deems necessary, and such other examinations of a registrar's transactions as the Minister of Finance may require, and
- (b) when and to the extent required by the Minister of Finance, participate in the destruction of any redeemed or cancelled securities or unissued reserves of securities authorized to be destroyed under the *Financial Administration Act*,

and he may, by arrangement with a registrar, maintain custody and control, jointly with that registrar, of cancelled and unissued securities.

Improper retention of public money

10. Whenever it appears to the Auditor General that any public money has been improperly retained by any person, he shall forthwith report the circumstances of the case to the President of the Treasury Board.

Inquiry and report

11. The Auditor General may, if in his opinion such an assignment does not interfere with his primary responsibilities, whenever the Governor in Council so requests, inquire into and report on any matter relating to the financial affairs of Canada or to public property or inquire into and report on any person or organization that has received financial aid from the Government of Canada or in respect of which financial aid from the Government of Canada is sought.

Advisory powers

12. The Auditor General may advise appropriate officers and employees in the federal public administration of matters discovered in his examinations and, in particular, may draw any such matter to the attention of officers and employees engaged in the conduct of the business of the Treasury Board.

Access to Information

Access to information

13. (1) Except as provided by any other Act of Parliament that expressly refers to this subsection, the Auditor General is entitled to free access at all convenient times to information that relates to the fulfilment of his or her responsibilities and he or she is also entitled to require and receive from members of the federal public administration any information, reports and explanations that he or she considers necessary for that purpose.

Stationing of officers in departments

(2) In order to carry out his duties more effectively, the Auditor General may station in any department any person employed in his office, and the department shall provide the necessary office accommodation for any person so stationed.

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| Oath of secrecy | (3) The Auditor General shall require every person employed in his office who is to examine the accounts of a department or of a Crown corporation pursuant to this Act to comply with any security requirements applicable to, and to take any oath of secrecy required to be taken by, persons employed in that department or Crown corporation. |
| Inquiries | (4) The Auditor General may examine any person on oath on any matter pertaining to any account subject to audit by him and for the purposes of any such examination the Auditor General may exercise all the powers of a commissioner under Part I of the <i>Inquiries Act</i> . |
| Reliance on audit reports of Crown corporations | 14. (1) Notwithstanding subsections (2) and (3), in order to fulfil his responsibilities as the auditor of the accounts of Canada, the Auditor General may rely on the report of the duly appointed auditor of a Crown corporation or of any subsidiary of a Crown corporation. |
| Auditor General may request information | (2) The Auditor General may request a Crown corporation to obtain and furnish him with such information and explanations from its present or former directors, officers, employees, agents and auditors or those of any of its subsidiaries as are, in his opinion, necessary to enable him to fulfil his responsibilities as the auditor of the accounts of Canada. |
| Direction of the Governor in Council | (3) If, in the opinion of the Auditor General, a Crown corporation, in response to a request made under subsection (2), fails to provide any or sufficient information or explanations, he may so advise the Governor in Council, who may thereupon direct the officers of the corporation to furnish the Auditor General with such information and explanations and to give him access to those records, documents, books, accounts and vouchers of the corporation or any of its subsidiaries access to which is, in the opinion of the Auditor General, necessary for him to fulfil his responsibilities as the auditor of the accounts of Canada. |
| Staff of the Auditor General | |
| Officers, etc. | 15. (1) The officers and employees that are necessary to enable the Auditor General to perform his or her duties are to be appointed in accordance with the <i>Public Service Employment Act</i> and, subject to subsections (2) to (5), the provisions of that Act apply to those officers and employees. |
| Public Service Employment Act—employer and deputy head | (2) The Auditor General may exercise the powers and perform the functions of the employer and deputy head under the <i>Public Service Employment Act</i> within the meaning of those terms in subsection 2(1) of that Act. |

**Public Service
Employment Act
—Commission**

Delegation

(3) The Auditor General may, in the manner and subject to the terms and conditions that the Public Service Commission directs, exercise the powers and perform the functions of that Commission under the *Public Service Employment Act*, other than its powers and functions in relation to the hearing of allegations by a candidate under sections 118 and 119 of that Act and its power to make regulations.

Sub-delegation

(4) The Auditor General may authorize any person employed in his or her office to exercise and perform, in any manner and subject to any terms and conditions that he or she directs, any of his or her powers and functions under subsections (2) and (3).

**Appointment of
Commissioner**

(5) Any person authorized under subsection (4) may, subject to and in accordance with the authorization, authorize one or more persons under that person's jurisdiction to exercise any power or perform any function to which the authorization relates.

15.1 (1) The Auditor General shall, in accordance with the *Public Service Employment Act*, appoint a senior officer to be called the Commissioner of the Environment and Sustainable Development who shall report directly to the Auditor General.

Commissioner's duties

(2) The Commissioner shall assist the Auditor General in performing the duties of the Auditor General set out in this Act that relate to the environment and sustainable development.

**Responsibility for
human resources
management**

16. The Auditor General is authorized, in respect of persons appointed in his or her office, to exercise the powers and perform the functions of the Treasury Board that relate to human resources management within the meaning of paragraph 7(1)(e) and section 11.1 of the *Financial Administration Act*, as well as those of deputy heads under subsection 12(2) of that Act, as that subsection reads without regard to any terms and conditions that the Governor in Council may direct, including the determination of terms and conditions of employment and the responsibility for employer and employee relations.

Delegation

16.1 (1) The Auditor General may authorize any person employed in his or her office to exercise and perform, in any manner and subject to any terms and conditions that he or she directs, any of his or her powers and functions in relation to human resources management.

Sub-delegation

(2) Any person authorized under subsection (1) may, subject to and in accordance with the authorization, authorize one or more persons under that person's jurisdiction to exercise any power or perform any function to which the authorization relates.

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| Contract for professional services | <p>16.2 Subject to any other Act of Parliament or regulations made under any Act of Parliament, but without the approval of the Treasury Board, the Auditor General may, within the total dollar limitations established for his or her office in appropriation Acts, contract for professional services.</p> |
| Classification standards | <p>17. Classification standards may be prepared for persons employed in the office of the Auditor General to conform with the classifications that the Auditor General recognizes for the purposes of that office.</p> |
| Delegation | <p>18. The Auditor General may designate a senior member of his staff to sign on his behalf any opinion that he is required to give and any report, other than his annual report on the financial statements of Canada made pursuant to section 64 of the <i>Financial Administration Act</i> and his reports to the House of Commons under this Act, and any member so signing an opinion or report shall indicate beneath his signature his position in the office of the Auditor General and the fact that he is signing on behalf of the Auditor General.</p> |
| | <h3>Immunities</h3> |
| Immunity as witness | <p>18.1 The Auditor General, or any person acting on behalf or under the direction of the Auditor General, is not a competent or compellable witness — in respect of any matter coming to the knowledge of the Auditor General or that person as a result of performing audit powers, duties or functions under this or any other Act of Parliament during an examination or inquiry — in any proceedings other than a prosecution for an offence under section 131 of the <i>Criminal Code</i> (perjury) in respect of a statement made under this Act.</p> |
| Protection from prosecution | <p>18.2 (1) No criminal or civil proceedings lie against the Auditor General, or against any person acting on behalf or under the direction of the Auditor General, for anything done, reported or said in good faith in the course of the performance or purported performance of audit powers, duties or functions under this or any other Act of Parliament.</p> |
| Defamation | <p>(2) For the purposes of any law relating to defamation,</p> <ul style="list-style-type: none">(a) anything said, any information supplied or any document or thing produced in good faith by or on behalf of the Auditor General, in the course of the performance or purported performance of audit powers, duties or functions under this or any other Act of Parliament, is privileged; and(b) any report made in good faith by the Auditor General in the course of the performance or purported performance of audit powers, duties or functions under this or any other Act of Parliament, and any fair and accurate account of the report made in good faith in a newspaper or any other periodical publication or in a broadcast, is privileged. |

Estimates

Estimates

19. (1) The Auditor General shall annually prepare an estimate of the sums that will be required to be provided by Parliament for the payment of the salaries, allowances and expenses of his office during the next ensuing fiscal year.

Special report

(2) The Auditor General may make a special report to the House of Commons in the event that amounts provided for his office in the estimates submitted to Parliament are, in his opinion, inadequate to enable him to fulfil the responsibilities of his office.

Appropriation allotments

20. The provisions of the *Financial Administration Act* with respect to the division of appropriations into allotments do not apply in respect of appropriations for the office of the Auditor General.

Audit of the Office of the Auditor General

Audit of the office of the Auditor General

21. (1) A qualified auditor nominated by the Treasury Board shall examine the receipts and disbursements of the office of the Auditor General and shall report annually the outcome of his examinations to the House of Commons.

Submission of reports and tabling

(2) Each report referred to in subsection (1) shall be submitted to the President of the Treasury Board on or before the 31st day of December in the year to which the report relates and the President of the Treasury Board shall lay each such report before the House of Commons within fifteen days after receipt thereof by him or, if that House is not then sitting, on any of the first fifteen days next thereafter that the House of Commons is sitting.

Sustainable Development

Purpose

21.1 In addition to carrying out the functions referred to in subsection 23(3), the purpose of the Commissioner is to provide sustainable development monitoring and reporting on the progress of category I departments towards sustainable development, which is a continually evolving concept based on the integration of social, economic and environmental concerns, and which may be achieved by, among other things,

- (a) the integration of the environment and the economy;
- (b) protecting the health of Canadians;
- (c) protecting ecosystems;
- (d) meeting international obligations;
- (e) promoting equity;
- (f) an integrated approach to planning and making decisions that takes into account the environmental and natural resource costs of different economic options and the economic costs of different environmental and natural resource options;

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| | (g) preventing pollution; and (h) respect for nature and the needs of future generations. |
| Petitions received | 22. (1) Where the Auditor General receives a petition in writing from a resident of Canada about an environmental matter in the context of sustainable development that is the responsibility of a category I department, the Auditor General shall make a record of the petition and forward the petition within fifteen days after the day on which it is received to the appropriate Minister for the department. |
| Acknowledgement to be sent | (2) Within fifteen days after the day on which the Minister receives the petition from the Auditor General, the Minister shall send to the person who made the petition an acknowledgement of receipt of the petition and shall send a copy of the acknowledgement to the Auditor General. |
| Minister to respond | (3) The Minister shall consider the petition and send to the person who made it a reply that responds to it, and shall send a copy of the reply to the Auditor General, within <ul style="list-style-type: none"> (a) one hundred and twenty days after the day on which the Minister receives the petition from the Auditor General; or (b) any longer time, where the Minister personally, within those one hundred and twenty days, notifies the person who made the petition that it is not possible to reply within those one hundred and twenty days and sends a copy of that notification to the Auditor General. |
| Multiple petitioners | (4) Where the petition is from more than one person, it is sufficient for the Minister to send the acknowledgement and reply, and the notification, if any, to one or more of the petitioners rather than to all of them. |
| Duty to monitor | 23. (1) The Commissioner shall make any examinations and inquiries that the Commissioner considers necessary in order to monitor <ul style="list-style-type: none"> (a) the extent to which category I departments have contributed to meeting the targets set out in the Federal Sustainable Development Strategy and have met the objectives, and implemented the plans, set out in their own sustainable development strategies laid before the Houses of Parliament under section 11 of the <i>Federal Sustainable Development Act</i>; and (b) the replies by Ministers required by subsection 22(3). |

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| Commissioner's report | (2) The Commissioner shall, on behalf of the Auditor General, report annually to Parliament concerning anything that the Commissioner considers should be brought to the attention of Parliament in relation to environmental and other aspects of sustainable development, including |
| | (a) the extent to which category I departments have contributed to meeting the targets set out in the Federal Sustainable Development Strategy and have met the objectives, and implemented the plans, set out in their own sustainable development strategies laid before the Houses of Parliament under section 11 of the <i>Federal Sustainable Development Act</i> ; |
| | (b) the number of petitions recorded as required by subsection 22(1), the subject-matter of the petitions and their status; and |
| | (c) the exercising of the authority of the Governor in Council under subsections 11(3) and (4) of the <i>Federal Sustainable Development Act</i> . |
| Duty to examine | (3) The Commissioner shall examine the report required under subsection 7(2) of the <i>Federal Sustainable Development Act</i> in order to assess the fairness of the information contained in the report with respect to the progress of the federal government in implementing the Federal Sustainable Development Strategy and meeting its targets. |
| Duty to report | (4) The results of any assessment conducted under subsection (3) shall be included in the report referred to in subsection (2) or in the annual report, or in any of the three additional reports, referred to in subsection 7(1). |
| Submission and tabling of report | (5) The report required by subsection (2) shall be submitted to the Speakers of the Senate and the House of Commons and the Speakers shall lay it before their respective Houses on any of the next 15 days on which that House is sitting after the Speaker receives the report. |

Appendix B Reports of the Standing Committee on Public Accounts to the House of Commons, 2011–12

The following reports have been tabled since our November 2011 Report went to print. They are available on the website of Canada's Parliament (www.parl.gc.ca).

41st Parliament, 1st Session

Report 1—Certificate of Nomination of Michael Ferguson to the position of Auditor General of Canada (Adopted by the Committee on 2 November 2011; presented to the House on 3 November 2011)

Report 2—Chapter 4, Programs for First Nations on Reserves, of the 2011 Status Report of the Auditor General of Canada (Adopted by the Committee on 21 November 2011; presented to the House on 6 February 2012)

Report 3—Chapter 3, Internal Audit, of the 2011 Status Report of the Auditor General of Canada (Adopted by the Committee on 12 December 2011; presented to the House on 8 February 2012)

Report 4—Chapter 2, G8 Legacy Infrastructure Fund, of the Spring 2011 Report of the Auditor General of Canada (Adopted by the Committee on 15 March 2012; presented to the House on 28 March 2012)

Report 5—Chapter 1, Financial Management and Control and Risk Management, of the 2011 Status Report of the Auditor General of Canada (Adopted by the Committee on 15 March 2012; presented to the House on 2 April 2012)

Report 6—Chapter 3, Reserve Force Pension Plan—National Defence, of the Spring 2011 Report of the Auditor General of Canada (Adopted by the Committee on 15 March 2012; presented to the House on 4 April 2012)

Report 7—Main Estimates 2012–2013: Vote 20 under FINANCE (Adopted by the Committee on 17 May 2012; presented to the House on 30 May 2012)

Report 8—Public Accounts of Canada 2011 (Adopted by the Committee on 15 May 2012; presented to the House on 6 June 2012)

Appendix C Costs of Crown corporation audits conducted by the Office of the Auditor General of Canada

The Office is required, under section 147 of the *Financial Administration Act*, to disclose its costs incurred in preparing annual audit (Exhibit C.1) and special examination reports on Crown corporations.

An annual audit report includes an opinion on a corporation's financial statements and on its compliance with specified authorities. It may also include reporting on any other matter deemed significant.

A special examination determines whether a corporation's financial and management control and information systems and its management practices provide reasonable assurance that

- assets have been safeguarded and controlled;
- financial, human, and physical resources have been managed economically and efficiently; and
- operations have been carried out effectively.

In 2011–12, the Office completed the special examination of two Crown corporations. The costs incurred are in the following table:

| | |
|--|-----------|
| Canadian Race Relations Foundation | \$467,021 |
| Public Sector Pension Investment Board (joint examination) | \$482,059 |

Exhibit C.1 Cost of preparing annual audit reports for fiscal years ending on or before 31 March 2012

| Crown corporation | Fiscal year ended | Cost (\$) |
|---|-------------------|-----------|
| Atlantic Pilotage Authority | 31.12.11 | 120,064 |
| Atomic Energy of Canada Limited (joint audit) | 31.03.12 | 721,909 |
| Blue Water Bridge Authority | 31.08.11 | 195,765 |
| Business Development Bank of Canada (joint audit) | 31.03.12 | 493,166 |
| Canada Council for the Arts | 31.03.12 | 295,715 |
| Canada Deposit Insurance Corporation | 31.03.12 | 232,015 |
| Canada Development Investment Corporation (joint audit) | 31.12.11 | 207,505 |
| Canada Employment Insurance Financing Board | 31.03.12 | 102,874 |
| Canada Hibernia Holding Corporation (joint audit) | 31.12.11 | 101,078 |
| Canada Lands Company Limited | 31.03.12 | 844,426 |
| Canada Mortgage and Housing Corporation (joint audit) | 31.12.11 | 595,513 |
| Canada Post Corporation (joint audit) | 31.12.11 | 761,613 |
| Canadian Air Transport Security Authority | 31.03.12 | 657,275 |
| Canadian Broadcasting Corporation | 31.03.12 | 1,069,765 |
| Canadian Commercial Corporation | 31.03.12 | 260,759 |
| Canadian Dairy Commission | 31.07.11 | 213,396 |
| Canadian Museum for Human Rights | 31.03.12 | 174,883 |
| Canadian Museum of Civilization | 31.03.12 | 140,990 |
| Canadian Museum of Immigration at Pier 21 | 31.03.12 | 140,643 |
| Canadian Museum of Nature | 31.03.12 | 169,179 |
| Canadian Race Relations Foundation | 31.03.12 | 183,112 |
| Canadian Tourism Commission | 31.12.11 | 274,172 |
| Defence Construction (1951) Limited | 31.03.12 | 99,499 |
| Enterprise Cape Breton Corporation | 31.03.12 | 327,481 |
| Export Development Canada | 31.12.11 | 1,227,909 |
| Farm Credit Canada | 31.03.12 | 764,631 |
| Federal Bridge Corporation Limited, The | 31.03.12 | 159,160 |
| First Nations Statistical Institute* | N/A | N/A |
| Freshwater Fish Marketing Corporation | 30.04.11 | 369,766 |
| Great Lakes Pilotage Authority | 31.12.11 | 143,889 |
| International Development Research Centre | 31.03.12 | 200,338 |
| Jacques-Cartier and Champlain Bridges Incorporated, The | 31.03.12 | 208,849 |
| Laurentian Pilotage Authority | 31.12.11 | 114,222 |
| Marine Atlantic Inc. | 31.03.12 | 362,198 |
| National Arts Centre Corporation | 31.08.11 | 237,232 |
| National Capital Commission | 31.03.12 | 345,724 |
| National Gallery of Canada | 31.03.12 | 218,168 |
| National Museum of Science and Technology | 31.03.12 | 161,937 |

*The First Nations Statistical Institute's annual audit report for the fiscal year ended 31 March 2012 has not yet been issued. Due to entity delays in preparation of financial statements, audit work leading to the issuance of the annual audit report for the fiscal year ended 31 March 2011 is ongoing.

Exhibit C.1 Cost of preparing annual audit reports for fiscal years ending on or before 31 March 2012 (continued)

| Crown corporation | Fiscal year ended | Cost (\$) |
|--|-------------------|-----------|
| Old Port of Montreal Corporation Inc. | 31.03.12 | 279,472 |
| Pacific Pilotage Authority | 31.12.11 | 94,786 |
| Parc Downsview Park Inc. | 31.03.12 | 303,239 |
| Public Sector Pension Investment Board (joint audit) | 31.03.12 | 545,114 |
| PPP Canada Inc. (joint audit) | 31.03.12 | 143,209 |
| Ridley Terminals Inc. | 31.12.11 | 225,883 |
| Royal Canadian Mint | 31.12.11 | 650,862 |
| Seaway International Bridge Corporation Ltd., The | 31.03.12 | 107,874 |
| Standards Council of Canada | 31.03.12 | 103,974 |
| Telefilm Canada | 31.03.12 | 242,860 |
| VIA Rail Canada Inc. | 31.12.11 | 863,587 |

Report of the Auditor General of Canada to the House of Commons

Matters of Special Importance

Main Points—Chapters 1 to 7

Appendices

Planning the Use of Professional Service Contractors

Grant and Contribution Program Reforms

Protecting Canadian Critical Infrastructure Against Cyber Threats

Transition of Ill and Injured Military Personnel to Civilian Life

Real Property—National Defence

Transfer Payments to the Aerospace Sector—Industry Canada

Long-Term Fiscal Sustainability—Finance Canada

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